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Regulation

Sept/Oct 1981 AEI Journal on Government and Society

The New International Regulation

A Global Straitjacket

Richard Berryman and Richard Schifter

Has Reagan Dropped the Ball?

Robert W. Crandall

Nursing the Railroads Back to Health

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Does Overregulation Cause Underregulation?

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Unsnarling the Grant System

Claude E. Barfield, Jr.

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Letters

We welcome letters from readers, particularly commentaries that reflect upon or take issue with material we have published. The writer's name, affiliation, address, and telephone number should be included. Because of space limitations, letters are subject to abridgment.

White House Oversight

TO THE EDITOR:

George Eads ("Harnessing Regulation: The Evolving Role of White House Oversight," *Regulation*, May/June 1981) thoughtfully raises several issues concerning the Task Force on Regulatory Relief and President Reagan's Executive Order 12291. Eads correctly perceives the paradox of giving new substantive and oversight responsibilities to the Office of Management and Budget's Office of Information and Regulatory Affairs (OIRA) while limiting its staff resources and leaving the incentives of the agencies unchanged. Eads also claims that there may be less chance for public participation under the new executive order. I disagree with the latter observation; in addition, I believe the executive order is already having some salutary effects not discussed in Eads's article.

The executive order has caused all parties involved in regulatory decisions to sharpen their data bases, analytic tools, documentation, and presentations. Hundreds of parties with new or reawakened interest in the regulatory process have responded to the task force's request for information. During this "phase-in" period there has been *more* public participation, not less; it is more broadly based and seems to be more open; furthermore, some responses, while not presenting complete benefit-cost analyses, have provided agencies with helpful insights in specific substantive areas. Industry frequently possesses much of the data base needed for regulatory analysis, some of which it considers proprietary and thus would not normally volunteer. . . .

Wilbur A. Steger,
CONSAD Research Corporation

TO THE EDITOR:

Many of the changes made by the new executive order were either implicit in the Carter approach or are attempts to improve on the deficiencies of that system. Carter splintered regulatory oversight among many groups, so that no central entity could develop a regulatory policy to guide individual agency decisions. The new Office of Information and Regulatory Affairs at least has the *capability* to do so; moreover, the mere existence of a single office makes possible an accountability that was necessarily absent under the former approach. If problems do develop, as Eads fears, the political system will know precisely where to look to take corrective action.

Nor is there any particular reason to think that OIRA is about to collapse of its own weight. Eliminating the redundancies and conflicts of the earlier decentralized approach will save needed resources. The new functions, such as assessing alternative regulatory approaches under the Regulatory Flexibility Act, are closely aligned with existing ones and will not impose significant new staffing burdens.

The White House will, as before, depend on the agencies for analysis. Unlike before, however, OIRA will request interested parties to bring regulatory matters to its attention. It is hard to see how, as alleged, this will make the White House less able to keep track of regulatory problems. OMB will not just appraise agencies' regulatory analyses—which was RARG's chief power—but will also have the power to request additional work after quickly assessing the quality of analysis, thus reducing the need for long, time-consuming analyses in the first place except in the truly significant cases. As a result, the analytical burden should not increase as much as Eads appears to think.

The real concern of OIRA's critics appears to be that it intends to take its charge seriously and pursue regulatory oversight aggressively. While that may be taxing at times, it is certainly welcome. During the Carter administration, there was a widespread feeling that agencies regularly evaded their responsibility to carry out regulatory analysis by fraudulently finding that a regulation was not "major." If the agency did analyze the regulation and did a bad job of it, CWPS and RARG could comment on the sloppiness but were powerless to go much beyond that. And the Carter White House's signals were so ambivalent that agencies simply ignored analytical principles as they pursued their more parochial goals. When the showdown came on cotton dust, OSHA won and the lesson was clear.

Indeed, the very examples Eads uses to show creative use of White House oversight were battles that were *lost*. Moreover, in its last year, just when one would have thought its processes were maturing, RARG did not seem terribly active. Nor did any significant regulatory policy emerge in the difficult area of health and safety regulation. In short, it was easy to dismiss the Carter oversight process as ineffective.

The cost-benefit provision of the Reagan executive order differs more in emphasis than in kind from the Carter procedures. The latter directed the agencies to consider costs and benefits, quantify them, and then choose the least burdensome approach or explain in detail why it was rejected. Since that explanation would have to be extremely cogent to persuade a court that the rejection of the low-cost approach was not arbitrary or capricious, the theory of the Carter executive order was simply to use normal judicial review to force agencies to act cost-effectively. While the Carter administration "took pains to stress that its requirements should not be interpreted as subjecting rules to a 'cost-benefit test,'" the disclaimer seems more politically motivated than factually accurate.

I concur fully and heartily with two of Eads's major points. First, there seems to be too much emphasis on formal quantification of costs and benefits. Not only may such an effort be difficult and sometimes highly misleading, but it is also frequently not a cost-effective

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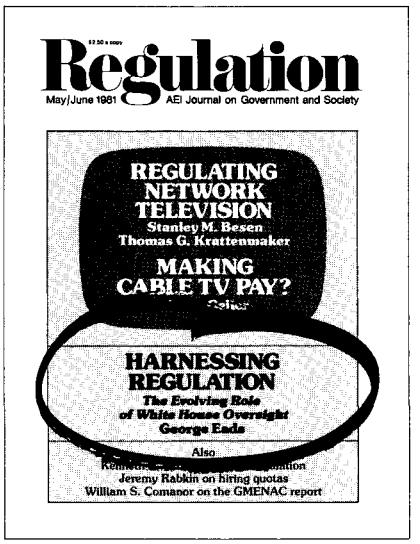
use of resources. The system should permit more flexibility and judgment. Second, since the first line of defense will always be the agencies, it is essential to encourage the development of sound regulatory proposals in the first instance. If, as Eads fears, OIRA becomes a clumsy, ax-wielding Queen of Hearts, good people will shun the agencies and everyone will lose—regulator and reformer alike. My hope is that individuals who are particularly well qualified to participate in regulatory decisions will now be taken more seriously in their agencies and hence be attracted to responsible positions. The test will be whether OIRA, as it shifts from the frenzy of getting things started to a normal operating mode, establishes good working relations with the agencies, or turns instead to an adversarial, anti-regulation stance. . . .

Philip J. Harter,
Kator, Scott, Harter & Heller



GEORGE EADS responds:

Philip Harter and I have very different views about what constitutes effective regulatory oversight. He places great faith in *form*: in clean organization charts, clear lines of authority, the ability of the oversight agency to demonstrate "wins." In his view, since the Carter process was organizationally "messy," since it never developed a clearly enunciated statement of "regulatory policy," and since those in the White House sometimes "lost" conspicuously, it was "ineffective."

His belief in the power of form is misplaced. There have been too many recent instances—energy comes immediately to mind—where the "solution" to a complex policy problem has been seen as principally organizational. The establishment of a centralized office with authority to review regulations does not, by itself, create the capability to develop and implement sensible regulatory policy. Such a capability only results from a proper matching of power with the ability to exercise it responsibly.

While the verdict is still out on the Reagan program, nothing that has occurred since I wrote my article calms the fears I expressed in it. Indeed, recent events suggest that I probably took far too optimistic a tone. As time has passed, OIRA's attention has increasingly focused on generating regulatory "body counts." OIRA staffers occupy their time "reviewing" (reading?) hundreds of petty regulations, 95 percent of which they declare to be "consistent with the President's program"—whatever that means. Meanwhile, original analysis by the White House staff has virtually ceased, and the backlog of issues raised by analyses performed by previous administrations is not being replenished. Agency analytical capabilities, crucial to the long-run success of any regulatory oversight process, are rapidly being dismantled. The word is being spread throughout the business community: "Forget analysis—it doesn't matter."

All of which makes the point raised by Wilbur Steger the more incredible. He refers to "hundreds of parties with new or reawakened interest in the regulatory process" who have responded to the vice-president's request for information, arguing that this has caused "all parties involved in regulatory decisions to sharpen their data bases, analytic tools, documentation, and presentations." He may be correct on the last point—presentations may have improved. But, by and large, these "wish lists" of regulations that one or another special interest wants to eliminate bear no more relationship to serious analysis than the wish lists we constantly received when I was in the White House. To refer to the process that produced these lists—and that has caused them to be uncritically forwarded to the agencies—as "public participation" is to debase the term.

Don't misunderstand me. Such lists can—and sometimes do—provide useful input for White House staffers seeking to oversee regulation. (I wish I had a dollar for every one we received.) But they should be carefully checked to determine whether their claims have merit. This requires the sort of independent analytical capability so sorely missing in the Reagan White House.

The Reagan oversight program deserves a chance to prove itself. And the Carter program certainly was far from perfect. But to be effective over the long pull, any oversight process must build capability, not destroy it. Unfortunately, thus far the Reagan process has demonstrated itself capable only of the latter. Those who run it would do well to recognize that its true test will be the staying power of the institutions it leaves behind. For regulation is not going to disappear.

Contrary to Harter's assertion, my fear is not that the Reagan process will succeed, but that it will fail, and do so in a way that confirms the worst fears of those who stress the dangers of White House oversight of regulation. That would be a tragedy.

Cable TV and Copyright Law

TO THE EDITOR:

In his argument for "true deregulation" of cable copyright ("Making Cable TV Pay? The Copyright Controversy," *Regulation,* May/June), Henry Geller calls for doing away with compulsory license and the Copyright Royalty Tribunal, and instead imposing full copyright liability on all cable systems operating in the 100 largest markets (while exempting all systems in smaller markets). He believes that eliminating the "cumbersome and impractical" CRT process would leave the pricing of copyrighted programs to the marketplace.

Now that the courts have upheld the Federal Communications Commission's repeal of its former restrictions on cable transmission, the Copyright Act of 1976, which did in fact contemplate the FCC's change in its rules, has a chance to work. It has been effective, and there is no reason why it should not be allowed to continue.

But Geller gives short shrift to one reason the compulsory license works: it eliminates the need for every cable system to negotiate with every copyright owner whose programming is to be retransmitted. Consider the burden involved in requiring more than 4,300 cable systems to negotiate individually for programming with hundreds, perhaps thousands, of copyright own-

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ers. The paperwork and manpower expended would be extraordinary and very costly.

Despite claims to the contrary, the marketplace has adapted to the compulsory license. The program supply industry has been unable or unwilling to quantify the impact of cable on program values, probably because of its relative insignificance.

Another indication that the marketplace has adjusted to compulsory license is the acceptance of superstations by the program supply industry. Program suppliers can refrain from selling to superstations to avoid widespread cable distribution. When WTBS in Atlanta emerged as a superstation in 1977, all but one of the major program syndicators refused to sell to that station. Now, however, all but one of the major syndicated program companies have sold programs to WTBS, and the last holdout has been negotiating with the superstation. Program suppliers have raised rates for programs sold to WTBS to reflect increased cable audience coverage, an example of the flexibility of the 1976 act.

We should not overlook the value of the compulsory license in serving the public interest. Three-quarters of the television markets in the United States, serving 35 percent of the television population, have no non-network TV stations. Cable helps balance this disparity by providing non-network programming outside big cities. Cable increases the public's viewing options. It is not asking too much for broadcasters and program producers to trade off just a little of the advantage they reap from the system to serve the public's interest in diverse programming.

Thomas E. Wheeler,
National Cable
Television Association

TO THE EDITOR:

One thing can be said about Henry Geller—he is persistent. Unfortunately, persistence in the pursuit of poor policy is no virtue. His proposal to require retransmission consent is Harold Stassen-esque in its appeal and in its recurrence. Merely repeating it over and over again, as he has done since the 1960s, does not cure its fatal policy flaws.

First, Geller assumes that, in a perfect market, cable systems would pay the same for the programming of a distant signal as broadcasters pay for their syndicated programming. He speaks of the differing percentage of their revenue that cable operators and broadcasters pay for non-network distant signal programming (1 percent and 30 percent respectively) as if this were a logical comparison. In fact, this is comparing apples and oranges. Cable has many channels (up to a hundred) to program. Distant signals may fill at most five or ten. The rest are filled with local broadcast channels exempt from copyright and gladly donated by local broadcasters, original programming produced by the cable system or local citizens (where the cable system is normally the copyright holder), and pay programming (like Home Box Office), which is subject to full copyright liability and for which cable bargains in the market.

Distant signals are, in short, only one small part of a cable operator's overall expense and generate only a part of a cable system's revenues. When all programming costs for larger cable systems are combined, they often claim 30 to 40 percent of gross revenues, a figure roughly equal to or more than the amount paid for programming by broadcasters.

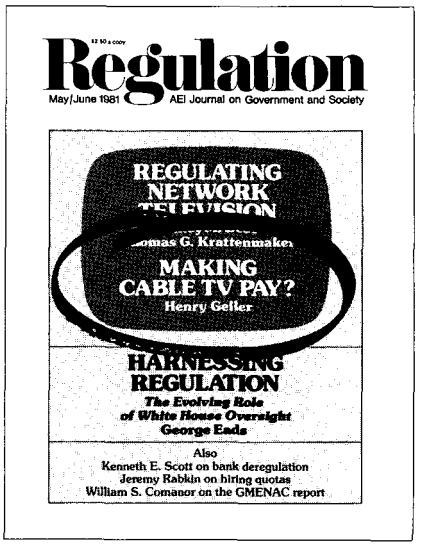
Another difference is that a broadcaster may capture up to a third of the audience in its city with its programming, while distant signals are watched by smaller portions of the cable audience, especially on multichannel systems. Some people may find the distant channel a compelling reason to subscribe to cable, justifying its carriage to the cable operator. But a straight comparison between a broadcaster's and a cable system's costs for that programming ignores the very different role that programming plays to each medium.

Second, Geller dismisses, but does not analyze, the importance of the FCC's extensive studies on the impact of the cable rules formerly restricting the number and content of distant signals a cable system could carry. The study prompting the FCC's recent deregulatory moves showed that local broadcasters and program producers would experience negligible impact as a result. People continue, by and large, to watch local stations even if they also watch distant stations. If audiences are not diverted by cable, local broadcast stations will continue to attract advertisers and revenues. Producers will continue to receive the same amount of income from syndicated programs.

In short, the FCC's studies showed that removing these outmoded rules would have no adverse effect on the program market. Geller has never been able to contradict this simple and compelling fact. . . .

The distant signal program market is only now beginning to evolve. The compulsory license is an essential element in its evolution. With Geller's system, this evolution would come to a screaming halt—as would, in many cases, the growth of the cable industry itself. To say that would be an unfortunate result may seem simplistic. But, unlike Geller's retransmission consent idea, it bears repeating.

Charles D. Ferris,
Mintz, Levin, Cohn, Ferris,
Glovsky, and Popeo, P.C.



HENRY GELLER responds:

I argued for adopting full copyright liability in the major markets while "grandfathering" cable operations in the smaller markets where change would be too disruptive and where there is, in any event, comparatively little revenue to programmers. In doing so, I made two main points:

(1) Cable, and it alone, is skewing the TV programming market by having the government intervene with a compulsory license and fee schedule.

(2) Such intervention is wholly unnecessary in light of the plethora of programming, both pay- and advertiser-supported, now available through satellite services.

Wheeler and Ferris ignore these points. They tacitly concede, therefore, that cable *is* skewing the market, when it could instead rely on satellite programming.

(Continues on page 60)

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Perspectives
on current developments

The Poor Man's Voucher?

Federal aid for the schooling of poor children —Title I aid, in educationist parlance—has been called the centerpiece of the Great Society education programs. Now proposals are circulating on Capitol Hill to make it the centerpiece of a policy of family choice in education—by "voucherizing" the program and letting poor children take the money with them to any public or private school they wish.

Title I puts up the money for school districts with high concentrations of poor children to hire experts and paraprofessionals for "compensatory" education, including testing, and other services to poorer students. In theory, at least, it attends to poor children not because they are poor but because poverty is a convenient proxy for low educational achievement; in practice, however, the program's supporters have rebuffed efforts to target the money specifically to low achievers. School officials frequently complain that the grant bureaucracy is not only cumbersome but also encourages them to segregate poor students from their classmates in order to ensure that no Title I funds are spent on the latter. Still, Congress has been unwilling to fold the program into a block grant, fearing that under that approach funds would be divided among schools without regard to need.

At around $3 billion a year, Title I is larger than all the other federal elementary and secondary school aid programs put together. According to a Department of Education study, no less than 16 million disadvantaged children, nearly one-third of all those of school age, are eligible for Title I services. Only 11 million of them live in eligible *areas*, however, and of these only about 5 million actually receive services. Private and parochial school students make up 3.5 percent of this sum, much less than would be their share if the money were allocated evenly among the poorest children. It is not difficult to see why: the federally financed services may not be dispensed in parochial school buildings, although students can sometimes hike over to the local public school to get them. (Another part of Title I pays for services to children in institutions and foster homes; it is thought less likely to be voucherized.)

Turning grants into vouchers would seem logical for an administration that already favors tuition tax credits as a step toward family choice in education. At the same time, it would face down three of the main arguments against tax credits: it would have no effect on the federal budget, would specifically help the poor, and would encourage integration and diversity in private schools.

"Mini-vouchers," as transferable Title I grants are sometimes called, were first proposed in detailed form by Berkeley law professor Stephen Sugarman in 1977. There has been little direct experience with them: the federally sponsored voucher experiment at Alum Rock, California, included a variant of the idea, but ended before any conclusive results emerged (although teachers reportedly "beat the bushes" to find poor children to enroll). Higher education, of course, has long operated on a voucher-like basis, and several federal programs specifically help with the college training of the disadvantaged.

The plan's most egalitarian feature—that it treats all poor children alike, no matter where they live or go to school—is also its greatest hurdle in implementation. Under the current arrangement, the federal government spends an average of $600 in aid on behalf of 5 million poor children, and nothing at all on behalf of another 11 million. Thus under a voucher plan, either additional billions would have to be spent bringing every school up to the highest current subsidy level per student, or eligibility would have to be tightened so as to restrict aid to the poorest families, or subsidies

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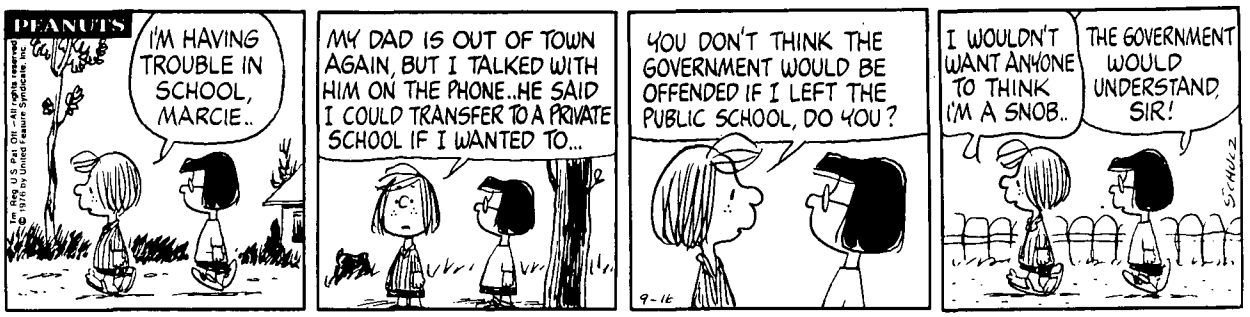
PEANUTS
I'M HAVING TROUBLE IN SCHOOL, MARCIE..
MY DAD IS OUT OF TOWN AGAIN, BUT I TALKED WITH HIM ON THE PHONE..HE SAID I COULD TRANSFER TO A PRIVATE SCHOOL IF I WANTED TO...
YOU DON'T THINK THE GOVERNMENT WOULD BE OFFENDED IF I LEFT THE PUBLIC SCHOOL, DO YOU?
I WOULDN'T WANT ANYONE TO THINK I'M A SNOB..
THE GOVERNMENT WOULD UNDERSTAND, SIR!
SCHULZ

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would have to be set at a lower level of $200 or so a student. Either of the last two courses would cut the amount now given to some schools.

Proponents of the scheme are thinking of sidestepping such issues by letting each state decide how to divvy up the voucher money within its boundaries. At its most gradualist, this approach would even let states distribute Title I money in its current form instead of as vouchers. (States that kept the current Title I distribution would presumably also keep the regulations that go along with it.) This alternative would, however, risk allowing fifty state bureaucracies to displace the present federal one.

One even milder approach that has occasionally been suggested is to replace the present complex funding formulas with "capitation" grants, giving a certain sum to each school district for each poor student enrolled there. Unlike the voucher plan, this proposal would do little to advance the cause of family choice, since students would still not be free to take the money wherever they chose. But it would assure every poor student—so long as he went to a public school—a subsidy of similar size, and it would implicitly proclaim that the government was interested in supporting students rather than school administrations. Perhaps for these very reasons, local officials have never appeared enthusiastic about the idea, despite the seeming advantage of being able to dispose of the grants in any way they wish.

It will be interesting to see how the opponents of tuition tax credits react to the idea of a voucher only for the poor. It stands their usual argument on its head. Will they now warn that student flight by the newly empowered poor will lead to a "two-class" school system, with poor children enjoying their private school preserve while the public schools become a "dumping ground" for the middle class?

When Patients Know What's Good for Them

Can patients know too much for their own good? That seems to be the issue in the controversy over the Food and Drug Administration's proposed rule on patient package inserts. The FDA is seeking to require drug makers to provide detailed data, for inclusion along with each prescription, describing to consumers the effect and proper usage of the drugs they take. The agency itself would prepare a model insert for each drug. Until now such directions for use have been required only for over-the-counter drugs and a few "elective" prescription drugs, such as oral contraceptives and estrogens. Not too long ago, in fact, makers of most prescription drugs risked charges of mislabeling if they furnished such information directly to consumers.

Initially the FDA wanted a highly ambitious scheme covering more than 300 drugs. But after criticism from President Carter's regulatory review panel, it settled on a three-year pilot program covering only ten frequently prescribed drugs that have serious side effects, drug interaction problems, or complicated dosage instructions. The ten drugs include varieties of tranquilizers and painkillers, cholesterol-lowering drugs, and drugs to combat irregular heartbeat, ulcers, loss of skin color, epilepsy, high blood pressure, and nausea in pregnancy.

The rule was adopted late last year, but the incoming Reagan administration's regula-

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tory task force held it up before it could go into effect and targeted it for review. A number of organizations led by the Health Research Group filed suit against the delay on April 8, charging that failure to provide package inserts to consumers constituted mislabeling. A federal court recently dismissed the case in order to give the FDA six months to review the program, after which the court may reopen the case. This will put the review of the rule on a faster track than other rules targeted by the task force.

The goal of the package insert rule, as of most information-based regulation, is not merely to disseminate information to consumers but to change their behavior. In theory, better information can help consumers avoid three major problems with drug use:

- *Patient noncompliance.* In some drug regimens, the dose must be continued after all symptoms have disappeared; in others a missed dose must be made up in a particular manner. Many drugs are incompatible with certain foods, with alcohol, with sunbathing, or with driving a car. Patients who have clearly written dosage instructions are more likely to comply with proper procedure. They may also avoid addiction and overdose problems.
- *Adverse side effects.* Some serious side effects start with mild symptoms, such as a rash, that the patient is likely to ignore. Drug information can alert patients to the importance of these symptoms.
- *Contraindications.* Some symptoms or conditions that make the use of a drug unwise or unsafe are more easily or more quickly identified by patients than by physicians. This is particularly true in the case of prolonged therapy, where the patient may develop the condition long after the drug is prescribed. If, for example, a drug should not be used in the first trimester of pregnancy, written advice to that effect contained in the drug package might prevent harmful use before a treating physician could do so.

According to some estimates, patient noncompliance costs $2 billion a year in added medical bills, and adverse reactions cost $156 million to $520 million a year. The agency also asserts that these problems account for a significant share of the lost workdays associated with acute conditions, which cost $9.1 billion a year. Against this are the measure's direct costs, estimated at $21 to $80 million a year—not large for a major regulatory program. Why, then, has this one run into such strong opposition, not only from drug manufacturers, but also most pharmacists and many doctors? Why has it made the Commerce Department's twenty-most-burdensome-regulations list?

The critics fear the rule for the same reason that a burgeoning "informed consent," or "patients' rights," movement favors it: because it will tend to encourage patients to take the curative process into their own hands, rather than trust in their physicians. The resulting change in the doctor-patient relationship, with its consequences for both patient health and the nature of the medical profession, is an indirect effect of sufficient magnitude to swamp the direct benefits and costs of the rule.

Both supporters and opponents agree that consumers are likely to ask their doctors more questions about drug therapy after reading the inserts. The extra time taken to answer questions raised by the inserts is not costless; it is now used to treat other patients. Critics worry that physicians will wind up correcting unnecessary misunderstandings, allaying fears of serious but rare side effects, cajoling needlessly frightened patients into continuing valuable drug therapy, and trying to distinguish the symptoms that some patients will develop from real contraindications or side effects.

It should be noted that a provision of the regulation gives doctors the right to request that the insert be omitted from a particular patient's prescription. Even with this safety clause, however, it is not clear that package inserts would reduce the medical cost figures cited by the FDA. If consumers are to benefit, they must read, understand, and retain the information, and then act appropriately, sometimes after quite a bit of time has elapsed. At each step along the way, fewer and fewer consumers can be expected to participate. Moreover, some adverse reactions have quick and irreversible onsets which cannot be minimized by consumer vigilance. And encouraging patients to take a more active and critical attitude toward their therapy may increase noncompliance by those who are frightened by the inserts' warnings or simply feel that they know better than anyone else what is good for them.

A few retail pharmacists support the rule, hoping to move the practice of retail pharmacy

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In Brief–

The Metamorphosis of Martyred Mice. *The Journal of Irreproducible Results,* a scientific humor magazine, offers the following definition: "The mouse is an animal which, when killed in sufficient numbers under carefully controlled conditions, will produce a Ph.D. thesis." Or, they might have added, a regulation.

Missing: Two Million Handicapped Kids. The General Accounting Office has declared no less than 2 million handicapped children to be missing and unaccounted for—and the Department of Education is giving out big rewards for apprehending them. The department's Office of Special Education has estimated that over 6 million children, about one-eighth of all children of school age, are handicapped and therefore entitled to federally funded services. State education officials, however, have only been able to round up about 4 million, despite repeated exhortations from Washington to do better.

Contrary to what one might expect, the handicapped students found so far are not spread at all evenly across the country. Some states put twice as many of their pupils in the handicapped category as do others. GAO also found that some states have stretched eligibility rules to boost their "childcounts" (as they are infelicitously called), mindful of the $240 average annual bounty that the federal government is willing to pay for each child.

Why is there so much uncertainty as to who is handicapped and who is not? GAO notes that a large chunk of the handicapped estimate consists of very young children with speech disabilities, often minor ("e.g., they said 'wabbit' instead of 'rabbit' "), which tend to disappear in the course of a few years. Nearly all the rest are in the highly elastic categories "emotionally disturbed," "learning disabled," and mentally retarded. Blind and deaf children make up less than 1 percent apiece of the total.

We Owe It to Ourselves. In the days before Reaganomics—indeed before Nixonomics and even Trumanomics—the FDR braintrusters were wont to belittle the dangers of a large national debt by noting that, after all, we owe it to ourselves. That insight has found new application in an entirely unexpected context: pay raises for members of Congress.

By law, every four years the President proposes changes in basic salaries for high-level government executives, federal judges, and members of Congress. Either house of Congress can veto his proposal, but until 1977 neither one was obliged to vote on the matter. Thus Congress could snag itself a pay raise without so much as a vote in either house—a nice example of the dangers of the legislative veto device. When, in January 1977, Congress got a 30 percent raise by this look-ma-no-hands method, the public outcry was so great that the law was amended to require an official floor vote.

But while Congress could no longer raise its base pay without standing up to be counted, it could still pick up handsome cost-of-living increases incognito. Under a 1975 law, the pay of members of Congress, along with top federal executives and judges, was required to be increased annually by the same percentage as the average cost-of-living raise given to regular federal workers under another statute. That latter raise may take effect without a congressional vote (the legislative veto gimmick again), and even when a vote occurs it does not present the appearance, though it has the reality, of Congress's raising its own pay.

Until recently, there was only one hitch in this eminently satisfactory arrangement: even though, once cost-of-living raises were given to regular federal workers, the raises for Congress were automatic, money still had to be appropriated to *pay* them. Some curmudgeons would use annual appropriations bills as vehicles for forcing a floor vote on the congressional pay issue, and when forced to declare themselves, their colleagues would reject or reduce the hike.

That problem has now been solved. A provision of the continuing appropriations legislation for 1982, signed by the President on October 1, enacts a permanent appropriation, beginning in fiscal

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toward a "European" model—with the family pharmacist, rather than the physician, acting as the major adviser on drug use. But most oppose it—and not necessarily because they expect to spend a lot of money storing the inserts and disseminating them to consumers. Quite the opposite. Since it is less costly to insert package inserts by machine in a factory than by hand in a pharmacy, the cost advantage will shift in favor of unit-of-use packaging, which would allow drugs prescribed in standard doses to be dispensed by less highly trained personnel. Thus the program may hasten the demise of retail pharmacy as a professional practice.

Doctors and pharmacists are not, of course, the only sources of knowledge for consumers at present. Information similar to that in package inserts is currently available in book form, as small compendiums written for the lay population and widely available at low cost. But consumers make little use of these volumes. One reason is that since a drug is frequently marketed under several brand names, a com-

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1983, for the annual congressional pay increases "required" by the 1975 act. It was, after all, only fair —indeed, a matter of entitlement, as Rep. Whitten put it in the brief House discussion (it would go too far to call it a debate): "Well, the law . . . provides the increased pay. We in the Congress have just failed to appropriate for it. . . . It is my opinion, having read some of the cases having to do with entitlements, that . . . it must be paid. It is my judgment that in a class action suit, members of Congress could sue and a judgment would be rendered."

One would have thought that such a fine ethical and juridical sense of entitlement would have extended as well to federal executive officers and judges, who are entitled to annual cost-of-living pay raises under the very same 1975 act. Not so, however. *Their* appropriations will continue to be made annually. They, unlike the members of Congress, do not owe it to themselves.

Non-Carcinogen of the Month. The *Washington Monthly* reports that boxes of D-Con brand rat poison boast in large letters: "An exclusive blend of all-natural ingredients." No Delaney Clause problems for them.

Floaters' Rights. From progressive California, home of tenant's rights, comes word that a new front has been opened in the unceasing struggle against landlord exploitation. According to the *Wall Street Journal*, the Waterbed Manufacturers Association of Los Angeles has begun a crusade to prohibit landlords from dictating what kind of furniture tenants can have. The furniture in question? Waterbeds, of course—banned by five out of six landlords because of fears that the beds will spring a leak or fall through the floor.

The waterbed makers have appealed to legislators in California and elsewhere to outlaw this discrimination, and they report that the initial response looks "very good." "Anybody who discriminates against furniture is unfair," proclaims the association's president. "Such discrimination probably is unconstitutional and it constitutes cruel and inhuman treatment."

Whales Escape White House Oversight. The executive branch has been mildly opposed to writing into law the "regulatory impact analysis" (RIA) procedures now contained in Executive Order 12291. There are understandable reasons for its opposition. It wants to retain the flexibility to make its own changes in the future. It also fears that any changes added in the legislative process will be for the worse, and that legislation will open the door to judicial review of regulatory analysis.

A bill signed by the President October 9 suggests another good reason: What the Congress giveth, the Congress taketh away. Public Law 97-58, which alters the administration of the Marine Mammal Protection Act of 1972, includes a clause exempting rulemakings conducted under its provisions from the application of E.O. 12291. As Reagan noted when he signed the bill, that provision may interfere with powers conferred on the President not by Congress but by the Constitution itself. To some degree, at least, the President must be able to establish internal procedures—whether Congress approves or not—necessary for the performance of his duty to "take care that the laws are faithfully executed."

In this instance, the congressional exclusion of RIA procedures seems to have been based on motives congenial to Reagan administration deregulatory policies. (The rulemakings in question could adopt existing state restrictions, instead of promulgating new federal restrictions.) In the future, however, it is infinitely more likely that such provisions will result from attempts by congressional committees to insulate their pet programs from White House oversight. Congressional deregulators should have known better than to establish a precedent as troublesome as this one—especially since the executive order already permits OMB to waive those provisions of the order that might deter deregulation. The experience suggests that the President might want to leave his executive order on the books even should it be enacted word for word into statutory law; in one important respect, namely destructibility by legislative action, a statute is more fragile than an executive order based on the President's constitutional powers.

plete compendium may be confusing to lay readers, most of whom use only a few prescription drugs. Worse, drug information must be frequently updated. Overall, however, the likeliest explanation is that consumers typically believe that their physicians will provide them with all necessary information.

What about manufacturers? In other markets, producers usually disclose negative information to their customers for fear of court liability. In the case of prescription drugs, statutes and case law do force them to disclose information about the drug's proper use—but to the prescribing physician, not the patient. Injured patients have successfully sued when, as in the case of thalidomide, the drug was not safe and effective in its intended use, or when, as in the case of chloromycetin, the drug manufacturer failed to provide the physician with sufficient information. In fact, until the FDA's relatively recent imposition of package insert requirements for certain elective drugs, prescription drug manufacturers not only had no duty to disclose information to patients under

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the Food, Drug, and Cosmetic Act of 1938, but actually were thought to risk charges of mislabeling if they did so—because drug information was viewed as inherently too complex for patients to understand. Thus, government policy has swung in two generations from a virtual right of self-medication before 1938, to a highly paternalistic system thereafter, and now, if the new rule survives the review process, to a hybrid position.

Saving the Cities . . .

The search for new victims of oppression to protect and defend is, for most fans of activist government, a never-ending one. Never, however, had they picked a more unlikely target for their solicitude than when, as part of the Carter administration's "urban policy," they rushed to the aid of downtown business interests.

The Community Conservation Guidelines, issued by the White House in November 1979, attempted to shelter central business districts from the effects of competition by requiring review of any federal actions that might promote the flight of business to the suburbs. The rules were quietly dropped this past June, only a year and a half later, by the Reagan White House.

Why any policy would be needed to help downtown business might well seem a mystery. Main street businessmen have long been portrayed, in American literature and journalism, as among the chief nodes of local power. Recently, however, a specter has been haunting them—the specter of shopping malls.

Shopping malls are so ubiquitous nowadays that it is easy to forget what a recent invention they are. It has been only twenty-five years since the first "modern" enclosed mall, Southdale Shopping Center, opened near Minneapolis. The success of the malls is only partly due to the national love of the automobile and to physical advantages like climate control. "Little at the shopping centers is left to chance," writes University of Chicago historian Neil Harris. "Along with Disneyland, they were early experimenters in the separation of pedestrian and vehicular movement and the isolation of service activities from customers." They also pioneered innovative approaches to traffic congestion, lighting, and security.

One prime reason for their success is that they compete just as directly with local government as they do with downtown business. Nearly every tax-paid public servant one is likely to encounter while shopping downtown, from the street sweeper to the cop on the beat, is replaced in a mall by a private employee. Malls achieve the goals of zoning and city planning (uniform architectural style, traffic control, efficient use of space, the exclusion of unwanted activities) within a wholly voluntary setting. By contrast, City Hall increasingly is deeply involved in the newer downtown developments, providing tax-free financing and using condemnation powers to assemble small land parcels. Thus it should come as no surprise that the most vociferous supporters of the community conservation guidelines were not the downtown merchants (who often have branches in the malls anyway) but the downtown governments.

Obviously, it would be possible to review only a small proportion of all federal actions for "urban impact." The Carter administration's response to this problem was simple: agencies were required to review an action only if the chief elected official of the affected city so requested. Needless to say, suburban officials, some of whose constituents had moved to escape big-city government in the first place, found that feature somewhat irksome. Many of them were already complaining that they had little control over federal projects within their boundaries; now it appeared that federal officials were going to hand some of that control, not back to them, but to the mayor of the nearby Gotham.

One announced reason for the policy was to compensate the cities for the federal subsidies already being provided for suburban development. But it is doubtful that even public works construction programs favor the suburbs (to say nothing of income transfer and social service programs, which surely subsidize the cities). Highway construction is paid for mostly by suburban drivers through the gasoline tax, while urban public transit gets large federal subsidies. Grants from the Economic Development Administration and Farmers Home Administration finance some suburban projects but, overall, they tilt toward ur-

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ban and rural recipients. The vast array of mortgage subsidies and tax preferences for housing apply to owner-occupied units everywhere, including urban condominiums. All of these policies probably do encourage overuse of land, but blocking large-scale shopping projects might worsen this problem if, as developers predict, the alternative is a proliferation of small-scale stores and centers. Malls use less parking space than dispersed stores of similar capacity.

The Carter administration action followed a number of local battles between city governments and mall developers. The governor of Massachusetts had threatened to deny state highway access to any shopping mall competing with a city-backed development planned for the city of Pittsfield. A land use commission in Vermont had denied a permit to a development it said would take business away from downtown Burlington. Over in Canada, the provinces of Ontario, Nova Scotia, and Saskatchewan had all enacted "Main Street" laws, with similar purpose. Such local efforts tend to founder, however, because of the underlying economic trends. In Pittsfield, for example, the officially sponsored project was abandoned in the face of traffic worries and retailer indifference, despite a promised federal Urban Development Action Grant of $14.2 million. Moreover, the local efforts have been left on legally shaky ground by various court rulings that zoning cannot be used to curb competition.

The resort to federal guidelines, however, likewise had little visible effect. The Transportation Department did deny funds for an interstate highway bypass around Dayton and put severe restrictions on the last link of a beltway around Richmond, in order to make it more difficult for drivers to avoid the center city. But few if any proposed malls were canceled because of federal pressure.

The tentativeness of these and other moves toward federal control of land use probably reflects public resistance to the idea of a government policy determining where people should live, work, and shop. When the Boston city government decided to require its employees to live in the city, opponents of the requirement—recalling "forced busing"—came up with another pithy phrase: "forced living," they called it. "Forced shopping" is probably no more popular.

A certain cynical theory would have it that social trends never come to the attention of the government until they are past their peak. With regard to the present issue, the state of affairs in retail trade lends some credence to that theory. The trend toward suburban malls seems to be slowing down, most cities of any size already having been "malled out," in the developers' inelegant phrase. Meanwhile, downtowns are reviving nicely in some of the oldest cities—Boston, Philadelphia, Baltimore—led not by general retail trade but by specialties like tourism, art, entertainment, and the professions, and by stores catering to newly renovated inner-city neighborhoods.

. . . and Saving the Country

Even as the Reagan administration dismantles one government policy aimed at slowing suburban growth, it is busy erecting another—an "agricultural lands protection policy." This policy was part of the omnibus farm bill passed by the Senate September 18 with administration support and awaiting House action as of this writing. Like the guidelines on saving the cities, it provides for review of federal actions that might abet "unnecessary" sprawl—this time, actions that would encourage the conversion of farmland to other uses.

Just as the suburbs draw people and businesses from the city, so they draw land and greenery from the countryside. From 1967 through 1975, 675,000 acres of cropland were converted each year to nonagricultural purposes. This trend, like so many others, would have dire consequences if it continued indefinitely: there were only 415 million acres of cropland in 1977, and by about the year 2600, we would have paved (or at least sodded) over every last one of them, right down to the last beanstalk.

For the moment, however, there would seem to be little cause for alarm. The price of farm products has risen less rapidly than other prices since 1890, and only half as fast as consumer income. The actual amount of cropland harvested has been rising, not falling, going from 289 million acres in 1972 to 353 million acres in 1980. (The cropland total of 415 million acres includes fallow land, land on which crops

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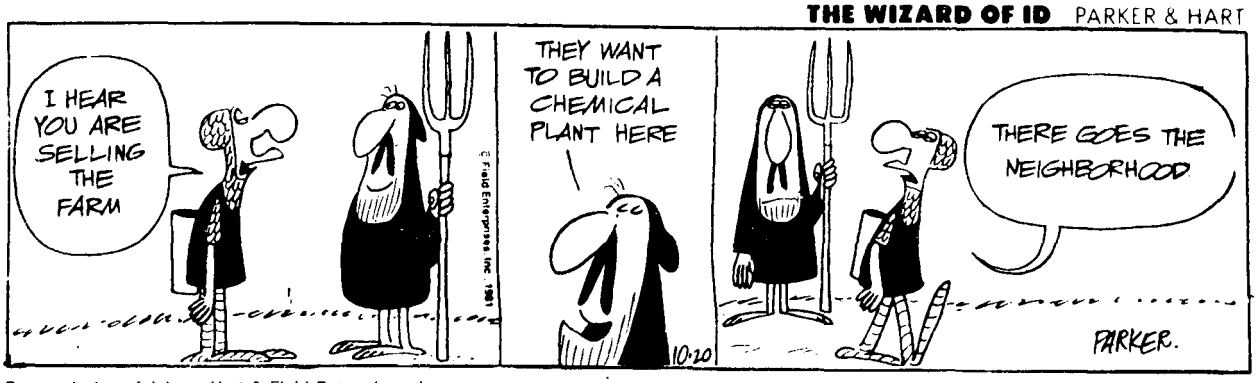
THE WIZARD OF ID PARKER & HART
I HEAR YOU ARE SELLING THE FARM
THEY WANT TO BUILD A CHEMICAL PLANT HERE
THERE GOES THE NEIGHBORHOOD
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have failed, and so forth.) Another 125 million acres are considered to have high or medium cropland potential. More land was newly brought under cultivation in the past decade than was lost to development, even while the suburbs were growing at a rapid clip. In fact, the suburbs could continue to grow at their current rate for more than a century before the last of this remaining potential cropland would be brought into production. Only then would the total farmland in use have to begin dropping. And long before then, of course, everyone in the nation would have moved to the suburbs.

Figures like these make a "farmland crisis" appear rather remote. Yet farmland preservation has become one of the hottest conservation issues, at both the federal and local level. Most states now give farms preferential property and estate tax treatment in order to discourage development. Four northeastern states and several local governments use state money to purchase development rights to farmland. Exclusive agricultural zoning is becoming more common. The cause is one that greatly attracts many local interests—no-growthers, new suburbanites who want to slam the door behind them, self-sufficiency buffs who fret that Massachusetts does not produce enough food for its own needs, and traditional politicos who cannot have overlooked the pork-barrel possibilities of discretionary subsidies and variances. Farmers themselves are more ambivalent. While flattered by the notion that farming is an especially virtuous activity, most do not care to lose their right to dispose of their land however they see fit.

Much of the impetus for federal action has come from the National Agricultural Lands Study, sponsored by the Department of Agriculture and the Council on Environmental Quality and released in January 1981. As an exercise in government planning, the study closely resembles the medical manpower study reviewed in these pages earlier this year (William S. Comanor, "Health Manpower and Government Planning: A Review of the GMENAC Report," *Regulation*, May/June 1981). Both reports projected current trends in supply and demand forward to future decades, with virtual disregard of the primary mechanism that alters (and equilibrates) supply and demand in our economic system: prices. Predictably, both reports found that major imbalances would arise, and went on to explain how government could set things right.

In the case of the farmland study, the most striking extrapolation was that of demand. Demand for gasohol, the study predicted, will require 15 to 23 million acres of corn by 1990; agricultural exports, which already account for one of every three acres harvested in this country, will nearly triple by the year 2000. Since the authors did not forecast large gains in yields per acre, they had to conclude that huge new amounts of cropland will be needed by 1999—between 77 and 113 million more acres, depending on crop yield assumptions.

Now *there* is a crisis! The latter figure would nearly exhaust the remaining potential cropland, and twenty years is a short time in which to bring every last scrap of arable land into production. If 113 million more acres of cropland must be found in a hurry, we may need much more than a new federal review mechanism: we may need to plant the nation's golf courses with sorghum and convert the President's Rose Garden to a pumpkin patch.

Fortunately, such drastic measures are unnecessary. If demand turns out to be as strong

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as the study projects, crop prices will rise, making it profitable to farm a given plot more intensively, lowering demand from all sources, and encouraging foreign countries to produce more. A massive increase in farm demand would also slow down farmland conversion, needless to say, since land prices would rise. But whatever the projections, the land lost to development would amount to no more than small change—less than might be lost to gasohol production alone.

That there is no farmland "crisis" does not necessarily mean that there are no unnatural pressures for development. When suburbanites move into a farming area, they often object to pesticide spraying, roaming animals, and farm sounds and smells in general, and then file suits or demand zoning changes to get their way. Local property taxes may also encourage conversion. And federal farm subsidies that encourage farmers to keep land in crops may or may not be outweighed by the range of federal and local subsidies for land development in general.

But a review process for farmland conversion can only indirectly combat the problem of development subsidies. It may well prevent some unwise government projects. The projects that are built anyway, however, will tend to be more costly—as the government reroutes highways, for example, to zigzag through swamps, up and down steep hillsides and across rocky fields in order to avoid Sunnybrook Farm. Meanwhile, instead of being "pulled" to stay in the cities, would-be suburbanites will be "pushed" to stay off the farm. Deregulation marches on.

Ford Motor Co. v. FTC: No Rule without a Rulemaking?

There is new reason to believe that some federal appellate judges fail to read *Regulation* closely. No sooner had it been pointed out in the pages of this magazine (Antonin Scalia, "Making Law without Making Rules," *Regulation*, July/August 1981) that, by and large, the law permits federal agencies to establish law and policy through case-by-case adjudication instead of rulemaking, than the U.S. Court of Appeals for the Ninth Circuit published its opinion in *Ford Motor Co.* v. *FTC*, saying that, by and large, the law does not permit federal agencies to establish law and policy through case-by-case adjudication instead of rulemaking.

Ten other federal agencies have joined in an *amicus* brief in support of the Federal Trade Commission's petition for rehearing in the case. As well they should. If the *Ford Motor* opinion stands, it will be a landmark decision in federal administrative law and a major barrier to agency action.

The case involved an FTC proceeding against Ford Motor Co., Ford Credit Co., and Francis Ford, Inc., an Oregon Ford dealership, complaining of the dealer's repossession practices. When repossessing a car, Francis Ford credited a debtor only with the car's wholesale value, keeping for itself any surplus over that price obtained in the resale. The FTC asserted that this policy, which was standard for the industry, constituted an unfair trade practice. Ford Motor and Ford Credit settled with the commission, but the feisty Oregon dealership contested the action. It lost. The commission issued a cease-and-desist order directing Francis Ford to end the practice. Francis Ford appealed to the courts, and won.

As the Ninth Circuit described the case, "the narrow issue . . . is whether the F.T.C. should have proceeded by rulemaking . . . rather than by adjudication." The Supreme Court has never found that to be needed; indeed, all three of its cases addressing the issue have affirmed the authority of agencies to select, within very broad limits, whichever form of proceeding they deem best for announcing new principles of law and policy. The famous *Chenery II* decision (1947) permitted the Securities and Exchange Commission to disapprove a reorganization of a utility company on the basis of a newly framed general prohibition of insider trading during the reorganization period. In *NLRB* v. *Wyman-Gordon* (1969) the Court allowed the labor board, in an adjudication concerning a union election, to establish and enforce a new requirement that the employer provide the union with employee names and addresses. And in *NLRB* v. *Bell Aerospace Co.* (1974) the Court held that the labor board could, in an adjudicative union certification proceeding, reverse its long-standing position

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that company "buyers" were "managerial employees."

In these cases the Court made it clear that the choice between rulemaking and adjudication as a way of making policy "lies primarily in the informed discretion of the administrative agency." The cases do suggest, however, that such discretion may be so abused as to warrant judicial reversal—for example, if persons suffer substantial adverse consequences from relying on prior agency policy or if fines or damages are imposed. Neither of these specifically mentioned factors was involved in the *Ford Motor* case: penalties would apply only for future violations of the cease-and-desist order, and there was no prior statement of FTC policy on which the affected industry had relied.

The Ninth Circuit, however, rested its decision on a new ground. "Ultimately," it said, "we are persuaded to set aside this order because the rule of the case made below will have general application. It will not apply just to Francis Ford." That is, on its face, an astounding holding. As the Supreme Court said in *Chenery,* an agency may use a "particular proceeding for announcing and applying a new standard of conduct." And as it said in *Wyman-Gordon* and reaffirmed in *Bell Aerospace,* "adjudicated cases may and do . . . serve as vehicles for the formulation of agency policies," and "generally provide a guide to action that the agency may be expected to take in future cases."

Aha! Perhaps *that* is what makes the *Ford Motor* case different! The FTC categorically declared that its holding would be binding on future cases—not just a "guide to action that the agency may be expected to take" or a precedent "subject to the qualified role of *stare decisis* in the administrative process," as *Wyman-Gordon* put it. Indeed, the FTC appended to its order against Francis Ford a "Synopsis of Determinations" that even read like a rule—with the apparent purpose, as the court noted, of advising other automobile dealerships of their new obligations. Is this the crucial distinction, then—that when an agency phrases its adjudication-formulated policy too categorically it becomes invalid?

Rather a precious distinction, certainly, exalting form over substance to a degree that is rare even in that world of form, the law. Moreover, such a prescription of proper adjudicatory form is hard to square with the Supreme Court's estimation that its own adjudications represent "the supreme law of the land." But finally and most conclusively, if the agency did exaggerate the categorically binding effect of its adjudication, it was clearly invited to do so by Congress.

Before 1973, the commission could impose a penalty for an unfair or deceptive trade practice only when, after it had adjudged the respondent guilty of the practice and issued a cease-and-desist order, the respondent failed to comply. One of the major features of the Magnuson-Moss Act of 1973 was its provision that if the commission determines in a cease-and-desist proceeding that "any act or practice is unfair and deceptive," it can thereafter impose a civil penalty upon *any* person (not just the one subject to the cease-and-desist order) engaging in "such act or practice" with "actual knowledge" that it is unfair or deceptive and unlawful. The obvious and well-known purpose of the provision was to enable the commission to impose penalties for the violation of general rules announced in adjudication. Which explains, of course, the "Synopsis of Determinations" appended to the commission's *Ford Motor* decision: it was to provide future violators with such "actual knowledge."

In other words, if there were ever a case in which Congress did *not* expect the agency to act through rulemaking, *Ford Motor* was it. The Magnuson-Moss provision described above necessarily *assumes* that the agency will pronounce in individual adjudications principles that "have general application." Yet it is precisely this which the Ninth Circuit says violates the law. Nor is it possible to explain the decision on the grounds that some constitutional prohibition against rulemaking-through-adjudication overcomes the evident congressional intent. It is hard to believe that the distinction between making a policy decision absolutely binding (if that is what the FTC sought to do), and making it binding only insofar as justified by the "qualified role of *stare decisis,*" is a distinction to be found in the Constitution. But even if it is, it is hard to see how the respondents in *Ford Motor* could benefit from it. If indeed it is unconstitutional to bind B on the basis of a principle enunciated in earlier litiga-

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Viewpoint

Robert W. Crandall

Has Reagan Dropped the Ball?

THE REAGAN ADMINISTRATION took office with a splendid opportunity to make major changes in federal regulation. Presidents Ford and Carter had helped clear the way by deregulating airlines and trucking and establishing White House review of major executive branch regulations. The public had increasingly come to associate regulation with declining productivity growth, persistent inflation, and mounting troubles for a number of basic industries. And Congress appeared on the verge of passing a strong general regulatory reform measure, and perhaps even sweeping changes in telecommunications and air pollution policy.

Unfortunately, despite the administration's fast start in this area, the prospects for substantive regulatory reform look dimmer today than they did nine months ago. In fact, the Reagan administration may have sacrificed much of its opportunity for major regulatory reforms—for at least three reasons. One is the pro-business tone set by its early pronouncements on the goals of its program. Another is that the White House is gambling too heavily on centralized review of rulemaking, rather than stressing fundamental change in major regulatory statutes. To date, Clean Air Act reform is the most serious casualty of this misplaced emphasis. And, finally, over at the Interstate Commerce Commission and the Federal Communications Commission, President Reagan's appointees seem inclined to reverse the movement toward deregulation in the trucking and broadcasting industries. If these unfortunate trends continue, the new administration will have forfeited any leverage it had in the regulatory arena.

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Relief or Reform?

We are less than twenty years away from Ralph Nader's *Unsafe at Any Speed*. The wave of regulatory legislation that followed the rise of "public interest" groups may have crested in 1970, but the undertow remains. If President Reagan's efforts to reform regulation are seen simply as a set of favors for corporations, a new wave of antibusiness populist sentiment may develop in the 1980s.

In its first utterances on regulatory policy, the administration has appeared willing to invite that risk. Again and again, it has announced regulatory proposals as "regulatory relief"—relief principally for industry, not consumers. While the administration's economists know that relieving industry of the more burdensome and unproductive regulatory impositions will lower consumer prices, the agencies do not advertise this as the most important effect. Instead they usually mention relief for the industry first, and then acknowledge—as a sidelight—that prices to consumers will be lowered.

In January, for example, the auto industry offered proposals for changing major environmental and safety standards affecting cars and trucks; and in April, the administration endorsed a number of these proposals in a document thoughtlessly entitled "Actions to Help the U.S. Auto Industry." Many of the items, such as eliminating the high-altitude emissions standards, seem quite sensible. But an impression has been left of wanting to do well by one's friends, not consumers in general.

The pattern of regulatory appointments also contributes to the problem of tone. For the most part, the agencies are now led by former industry employees or lobbyists, often persons

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who have no experience with the regulatory programs they now inherit. Some of these appointees seem to be overwhelmingly opposed to substituting market mechanisms for command-and-control regulation. Others are attempting to slow the pace of deregulation that built up under President Carter.

None of these appointments has succeeded in arousing the opposition as successfully as Secretary of Interior James Watt. But there are now enough doubts and concerns to encourage the antibusiness populists to reassemble. And many allies of deregulation may simply lose heart if the program is defended on the sole grounds that it's good for General Motors.

White House Oversight

So far the administration has dwelt single-mindedly on the process of reviewing regulations, while avoiding or mishandling opportunities for necessary changes in the underlying statutory basis of those regulations. Obviously, added White House muscle in reviewing the rules of executive branch agencies was needed. The Carter program lacked the political clout required, particularly after reformers had lost the battles on the smog standard and won only a modest victory on the cotton-dust standard promulgated by the Occupational Safety and Health Administration (OSHA). Reagan's program will, indeed, have more leverage over the regulators.

But this leverage is of limited use. If the statutes mandated programs that were demonstrably effective in extending life or cleaning up undesirable pollution, it might be sufficient to focus on streamlining the rulemaking process. If the only problem were poor management of a reasonable program, oversight by OMB's new Office of Information and Regulatory Affairs (OIRA) might be the only cure required. But the problems run much deeper: there is no solid evidence that these regulatory programs are even modestly effective. In most instances, the statutes mandate tasks so extensive that the agencies cannot meet deadlines, enforce the rules they set, defend themselves in court, and conduct retrospective evaluations of their effectiveness. More important, the statutes often forbid the use of a cost-benefit test in standard-setting, encourage economically inefficient regulations, and contain a strong bias against economic growth.

Most health, safety, and environmental regulators, for example, are empowered to control thousands upon thousands of different sources of a potential threat to health or safety. The Environmental Protection Agency (EPA) must regulate both new and existing chemicals, thousands of different sources of water pollution, hazardous wastes, motor vehicle emissions, stationary-source air pollution, pesticides, often making detailed determinations of "best" or "reasonable" technology for each type of source. The Food and Drug Administration admits that it is already so burdened with the licensing of new drugs that it cannot be equally thorough in evaluating older drugs. OSHA has similarly vast responsibilities. Administrative burdens of this sort overwhelm most of these agencies.

This is not the place to discuss the feasibility of cost-benefit analysis or the appropriate locus of a regulatory oversight procedure (on those matters, see "Harnessing Regulation" by George Eads, *Regulation*, May/June 1981). It is clear, however, that centralized review will not overcome poor agency performance. One measure of OIRA's success will be the degree to which it stimulates thorough and consistent analysis at the agencies. It is still too early to tell whether the agencies' analytical capabilities are getting better or worse. In most cases budget reductions and the usual problems of a political transition have combined to make hiring difficult. At best, all one can say is that nine months have not brought about revolutionary change at any of these agencies.

What gains have been made under the review process? There has been very little new regulation since the freeze was lifted in late April, with fewer than twenty-five major new regulations having emanated from the entire government in that time. Administrators apparently feel that inactivity (or at least caution) is *de rigueur* in the new Washington. Given current statutes, this willful failure to act will inevitably lead the pro-regulatory forces to sue the agencies in an effort to force action. But, surely, court-imposed deadlines are not preferable to the agency's own schedule.

Perhaps more distressing is the absence of any results from the review of existing regula-

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tory programs. Once again it is probably too early to judge, but it does not appear that existing rules are being scrutinized thoroughly. The task force's invitations to agencies to review existing rules have not yet been followed by agency action. There is no evidence that OSHA, EPA, the National Highway Traffic Safety Administration, or other agencies have begun the needed overhaul of programs under existing statutes or the drafting of new legislation.

Even with more time, it is extremely unlikely that OIRA's review process can make up for the poor design of regulatory statutes in the health, safety, and environmental areas. Without legislation, OIRA will only be nipping at the agencies' heels. And if the administration treats future legislative opportunities as it has treated the Clean Air Act, all hope may be lost.

Stumbling over Clean Air

Federal clean-air policy costs our society more than $20 billion a year and returns benefits that are modest at best. The rate of improvement in measured air quality has generally been lower since EPA was established in 1970 than it was in the decade of the sixties. Expensive controls on automobiles have not led to any discernible improvement in average smog levels. Most problems of interstate transport of dangerous air pollutants have not even been addressed. In short, there is little doubt that EPA's rules on clean air are among the most expensive and inefficient regulatory programs.

As luck would have it, the Reagan administration's first major legislative opportunity in the regulatory area was the 1981 deadline for reauthorizing the Clean Air Act. The possible targets for reforming this baroque statute are mind-boggling. One could begin by scrapping the ludicrous rule that all utilities use scrubbers and the tight technology-based standards for new sources (which discourage new investment), as well as most of the "nondegradation" policy (which is designed primarily to prevent industry from leaving the tired industrial regions of the country). Provision could be made for more trading of pollution-control obligations among firms so as to lower the overall cost of control. To reduce auto emissions and compliance costs, a program of relaxing new car standards, while taxing or buying up old cars, could be mandated. Finally, the illogical and exceedingly complicated penalties for noncompliance could be replaced by the simpler approach of penalizing excess emissions.

These options and a few others could have been assembled in a legislative package and sent to Congress by early spring, along with an analysis showing persuasively that they would produce cleaner air at much lower cost. Unfortunately, this did not happen. EPA spent months awaiting its new leadership and months more trying to draft a proposal. It finally gave up in August with the announcement that it would offer only "principles." Leaked copies of draft legislation were disowned, and the administration's stand was left obscure.

Because the effort was never accompanied by a clearly stated policy, the impression was created, perhaps inaccurately, that the White House wanted to relieve industry of compliance burdens, whatever the implications for clean air. EPA's espousal of the administration's new federalism led to a proposal for handing enforcement over to the states, a proposal widely viewed as a means of simply reducing compliance with EPA standards. There was discussion of loosening automobile standards but, when questioned, Administrator Gorsuch could not explain how that squared with air quality goals. With the administration suffering from the despoiler image of Secretary Watt, such a poorly articulated legislative strategy invited damaging misinterpretation. By late September, all chance of getting major Clean Air Act reform this year was gone.

Nor is there any sign of activity on other legislative fronts. For instance, in light of the recent Supreme Court decision on the cotton-dust standard, clearly the administration should now be pushing for major changes in the Occupational Safety and Health Act. In addition, legislation could be prepared to give state and local authorities the regulatory responsibilities that belong in their hands. The cumbersome and inefficient national program of registering hazardous wastes is one candidate for such an approach. Superfund financing for the clean-up of chemical dumps, a policy that will surely create all of the usual prob-

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lems of the federal pork barrel, could be replaced by a state program. Finally, properly structured state workmen's compensation laws could provide safety protection for workers more effectively and at less cost than the present system. If the administration is truly concerned with restoring federalism, it should be drafting legislative proposals now, while the constituency for such changes still exists. Unfortunately, in its handling of the Clean Air Act, it has squandered political capital and created serious doubts that reform of environmental, health, and safety regulation is possible.

Backsliding at the Independent Agencies

As if the above problems were not enough, the administration's appointments to at least two major independent agencies suggest that it does not wish to pursue economic deregulation as aggressively as did the Carter administration. At the Federal Communications Commission (FCC), and particularly at the Interstate Commerce Commission (ICC), there has been dangerous backsliding.

Throughout 1980, the Carter ICC moved vigorously to implement the Motor Carrier Act of 1980. Piggyback rates were deregulated and large numbers of trucking firms were allowed to enter new routes and markets. Trucking appeared on the way to total decontrol, a result clearly dictated by the evidence that rate-and-entry regulation is mainly a force for cartelizing truckers. The only major opponents were, of course, the truckers and the Teamsters.

During the 1980 campaign, candidate Reagan had made statements suggesting he would slow the pace of deregulation. He did not, however, say that a truckers' cartel was good policy. Once elected, he appointed a pro-regulation chairman to the ICC. Now it appears that the commission will attempt to constrain new operating authority for truckers and limit new entry into the industry wherever possible. ICC officials are talking about the "common carriage" responsibilities of carriers in language that smacks of the pre-1980 days when such notions were the excuse for cartelizing the industry. The new ICC chairman has even suggested that rate regulation and entry controls are necessary to ensure efficient energy use. The Reagan White House must be cringing.

At the FCC, the posture of the new chairman is less clear, but at least one major decision augurs poorly for competition in broadcasting. The FCC has rejected a proposal drafted during the Carter administration to reduce the spacing in the AM band so as to increase the number of radio stations in major markets. Other Carter proposals on radio deregulation, which are mostly devoted to reducing the licensee's formal obligation to act in specified ways, appear more likely to be implemented. They make eminent sense but, in the absence of a decision to increase competition by increasing the number of stations, they inevitably have a special interest taint.

These early episodes may not constitute a general trend. But the ICC alone has already done enough to undermine any administration claim to have restored as much economic activity as possible to the discipline of the market. If the ICC persists in recartelizing trucking, the White House will find itself on shaky ground should it begin to pursue deregulation in other markets, such as natural gas, international aviation, or the merchant marine.

IN POLITICS, AS ELSEWHERE, first impressions are important. Had the President been fainthearted when his tax or budget programs came before Congress, the prospects for his other policies would be much dimmer today. Similarly, if he allows his regulatory program to take on the appearance of goodies for business, he will lose the momentum for making much-needed changes in health, safety, and environmental policies.

Making a dent in the burden of regulation will take more than an enhanced regulatory review process. People will continue to demand safe work environments, clean water and air, and safe products, amenities that can be delivered without the incredible costs our current programs impose. But if the administration allows its EPA administrator to discard market alternatives in favor of technology-based standards, if the independent commissions seek to hold back deregulation, and if a few more months pass without important administration initiatives, the bold program of January will look very empty indeed. Then, as new problems grab the attention of busy legislators, regulatory reform may become the zero-based budgeting of the 1980s. ■

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The New International Regulation

A Global Straitjacket

Richard Berryman and
Richard Schifter

Lead the people by regulation and they will flee from you and lose all self-respect.

Confucius

IMAGINE THE FOLLOWING SCENARIOS:

- You are president of Company A, a U.S.-based multinational corporation that has already spent tens of millions on a novel process for mining the deep seabed. Millions more will be needed before commercial operations can begin and, even then, it will be years before the investment is recovered. But now a quasi-governmental international body says that your company will not be permitted to exploit the process commercially without first sharing its secrets with a competitor created and run by this very same international body.
- You are marketing manager in West Africa for B Corporation, a U.S. manufacturer of consumer products. For years you have routinely used computers to accumulate financial and marketing information and send it back to company headquarters. Suddenly you learn that the countries in which you operate will not allow computerized data to be sent abroad unless it is first reviewed by the host government. You protest and are told that such interference with your business is authorized in a multilateral agreement sponsored by the United Nations (UN).
- As chief executive officer of XYZ Pharmaceuticals of America, you take pride in your company's record for developing safe and beneficial drugs that have met the exacting standards of the Food and Drug Administration (FDA) and comparable foreign agencies, and have been marketed throughout the world. Now you are told that approval by na-

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tional agencies will no longer suffice. The World Health Organization is establishing an "international FDA" whose clearance will be required for all pharmaceuticals sold in countries acceding to its authority.

Unimaginable scenarios? Not if the new international regulators have their way. For in recent years, while Americans concerned about undue regulation have focused on our own government, a fast-proliferating assortment of international bodies have been moving to regulate various aspects of commercial, scientific, cultural, and political life worldwide. Little-heeded in the United States, even by those who keep track of foreign affairs, these efforts, if successful, could severely alter American life in ways that would be felt at home as well as abroad, and by U.S. industry and consumers alike.

The Genesis of the New International Regulation

Although not part of an explicitly coordinated global program, the international regulatory programs that have sprung onto the world scene during the past decade have a common source, a common body of principles, and common methods for attaining their goals. To be sure, there is nothing new about the concept of having an international body work out standards designed to govern particular areas of commerce. Such groups date back at least to the Hanseatic League of Medieval Europe. In their modern form, they range from the International Union for the Protection of Literary and Artistic Works and the Hague Conventions of the late nineteenth century to the International Telecommunications Satellite Organization and the Organization for Economic Cooperation and Development (OECD) of today. Such groups have been concerned with alleviating confusion and other difficulties arising in areas where nations rub up against each other —particularly maritime transportation, aviation, industrial property rights, meteorology, and trade. Typically, they have proceeded by drawing interested parties into an effort to draft minimum standards meeting common needs and acceptable to all of the parties concerned. Their objective has been to facilitate, rather than restrict, trade and, in so doing, to benefit all nations by benefiting none in particular.

In the 1960s and particularly in the 1970s, however, a number of countries that had only recently achieved independence began to see a new use for multilateral standard-setting bodies. The end of colonialism had not brought the expected better life, at least materially, for most of the so-called third world. Indeed, with the departure of expatriate armies and administrators, conditions in many new nations went from bad to worse. Nor was there much hope of quick improvement. UN and other multilateral development initiatives had failed to live up to expectations. Eastern and Western bilateral aid programs were viewed with suspicion. Multinational corporations and foreign investment in general were seen as exploitative. And few leaders in the third world were disposed to take the risks inherent in tackling head on the huge educational, cultural, and infrastructural problems that were so central to their countries' difficulties.

In this climate, the third world turned increasingly to multilateral organizations, particularly those within the UN complex, and to the idea of international regulation. Through such collective action, the third world nations, ever expanding in number, hoped to attain a power far exceeding what they might achieve individually or even regionally. And because those organizations operate on the principle of one-nation one-vote, they would provide the ideologically attractive trappings of democracy for attempts to fashion the world economy along egalitarian lines. Even more to the point, standard-setting bodies convened under the aegis of the various UN bodies could be counted on to produce majorities friendly to third world aims. Besides, those bodies were amply financed through substantial contributions from Western nations and, in contrast to most third world governments, were well supplied

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with the type of professional civil servant needed for tackling complex regulatory matters.

The movement to use international bodies as vehicles for transforming third world economies found one of its earliest concrete expressions in the United Nations Conference on Trade and Development (UNCTAD). Established in 1964 as a permanent body for formulating general rules on trade between the developed and less developed nations, with a view to aiding the latter's development, UNCTAD soon began interesting itself in "codes of conduct" strongly favorable to non-Western nations. It also served as the midwife for the birth of the UN Charter of Economic Rights and Duties of States, adopted in 1974 by a General Assembly vote of 120–6–10 (with the United States, Belgium, Denmark, West Germany, Luxembourg, and the United Kingdom voting "no"). The new international regulators have cited this charter, along with its call for a New International Economic Order arranged through UN-sponsored "Global Negotiations," to justify their schemes for recasting world economic relations.

The charter's "sovereign rights" will . . . be mostly enjoyed by the third world, while the "sovereign duties" will mostly belong to the so-called first world.

No consistent economic theory, save that of redistribution, underlies the charter. Its treatment of raw materials contrasts sharply with its treatment of technology: it would have the former fetch as high and the latter as low a price as possible. On the one hand, sovereign states should have an unrestricted right to form primary commodity cartels and are free to regulate foreign investment and multinational corporate activity. On the other hand, sovereign states must share the technology needed to exploit what is called the common heritage of mankind. The charter's "sovereign rights" will thus in practice be mostly enjoyed by the third world, while the "sovereign duties" will mostly belong to the so-called first world.

Among the areas in which the new international regulators have been most active in the seven years since the New International Economic Order was promulgated are the extraction of natural resources, the transfer of technology, multinational corporate conduct, shipping, exports and imports, news gathering, and the transmission of data via computer.

Natural Resource Extraction

The most celebrated of the new international efforts to regulate the extraction of natural resources is the draft treaty that the UN Conference on the Law of the Sea has been preparing since 1973. That draft treaty, echoing rhetoric first voiced by third world leaders, characterizes an area representing two-thirds of the earth's submerged lands and the resources therein as "the common heritage of mankind." To make this "common heritage" accessible to all peoples, the draft would create a major multilateral body, the Seabed Authority, and authorize it not only to decide who would mine in the area in question, but also to run its own seabed exploration and mining company and to control the activities of private competitors.

The proposed Seabed Authority outwardly resembles the UN in that both structures have an assembly, a council, and a secretariat. On the level of real power, however, the draft Law of the Sea treaty, would accord far less influence to the United States (and other free world nations) than does the UN Charter. Whereas the United States has permanent representation on the UN's Security Council (as have the United Kingdom and France), it would not be guaranteed a seat among the thirty-six members of the Seabed Authority's council, while the Soviet bloc would be guaranteed at least three. Despite this shift in representation, member nations would contribute to the Authority in proportion to their UN assessments—meaning the United States would pay roughly 25 percent of the total.

The provision that would create an entity designed to compete with private entrepreneurs from the developed world was included in the draft treaty at the urging of the Group of 77 (a third world coalition that now numbers more than 110 countries) and a handful of developed nations (most notably, Canada). This entity, known as the Enterprise, would carry out mineral exploration and recovery activities in the common heritage area under the Authority's direction and on its behalf. The Enterprise,

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which would be governed by a fifteen-member board elected by the Assembly, would transport, process, and market the minerals it recovered.

It is in the operations of the Enterprise that the Authority's regulatory pinch would be felt most clearly. Private companies that had invested heavily to develop the complex and costly technology needed for deep seabed mining would not only be forced to fund a competitor having preferential rights, but would even be required to train, do exploration work for, and secure a market for that competitor. Specifically, to ensure that the Enterprise enjoyed up-to-date technology and choice mining sites, the draft treaty forbids the Authority from licensing applicants to mine in the common heritage area unless two key conditions are met. First, the applicant would have to agree to provide its technology to the Enterprise or to developing nations on "fair and reasonable commercial terms and conditions" determined largely by the Authority alone, and also to agree not to use in the common area any technology it refused to transfer. Second, an applicant wishing to mine a particular site would have to identify a second site as well, either one of which the Authority could then reserve for the use of the Enterprise or developing nations. To ensure that these competitors had the funds needed to do business, signatory governments would have to provide the Enterprise with start-up capital in the form of loan guarantees and interest-free loans—in proportion to their UN assessments; and private firms engaged in mining the deep seabed would have to pay the Authority license fees, royalties, and a portion of their profits. Finally, to guarantee a market for the Enterprise's production (and as a concession to land-based mining interests, particularly in Canada), mining operations in the common area would not be permitted to market nickel in amounts beyond the projected growth in world nickel consumption for two decades following the treaty's effective date.

Private companies . . . would not only be forced to fund a competitor having preferential rights, but would even be required to train, do exploration work for, and secure a market for that competitor.

In June 1980, alarmed by the direction that the Law of the Sea Conference was taking and recognizing that U.S. companies (in consortia with private enterprises from other developed countries) had already invested hundreds of millions of dollars in developing deep seabed mining technology, Congress passed and President Carter signed the Deep Seabed Hard Minerals Resources Act. This act provides that the United States will not ratify any Law of the Sea treaty that does not (1) protect U.S. investments in deep seabed mining made before the treaty's effective date and (2) give all parties "assured and non-discriminatory access, under reasonable terms and conditions to deep seabed minerals." Furthermore, to protect the right of U.S. firms to secure a foothold before a treaty goes into effect, the act authorizes the National Oceanic and Atmospheric Administration to license U.S. firms for deep seabed exploration until January 1988 and, after that, to issue licenses for mining. (These provisions would of course be superseded by the treaty, should it be ratified.)

The 1980 act's assurances did not still the U.S. criticisms. In March 1981, before the opening of what was supposed to be the final session of the Law of the Sea Conference, the Reagan administration announced it would not carry out the Carter administration's agreement to conclude the treaty by May. In particular, the new administration criticized the treaty for discriminating against private mining enterprises, for inadequately protecting development investments made before the treaty's effective date, for failing to make any provision for the arbitration of disputes between the mining industry and governments, and for subjecting key U.S. interests to decisions made in a forum in which the U.S. vote would carry very little weight. Accordingly, the administration has been reviewing U.S. policy and formulating a position on proposed final negotiations scheduled for next March.

Other zones containing potentially important natural resources are the targets of international regulation as well. Treaties originating under UN auspices are now in effect for space and for the Antarctic. The Agreement Governing the Activities of States on the Moon and Other Celestial Bodies became effective in 1980

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by virtue of having been ratified by six member nations—Austria, Chile, France, Morocco, the Philippines, and Romania. Declaring that celestial bodies, too, are the common heritage of mankind, this agreement establishes an international regime to govern the exploration and extraction activities of (at least) those private entrepreneurs whose governments have signed up. Exactly how the countries involved are to "equitably share" the benefits of such activities, especially in view of an injunction to give special preference to developing nations, is yet to be worked out.

The U.S. Department of State and the National Aeronautics and Space Administration supported the draft space treaty throughout long negotiations that began in 1970. And even the U.S. aerospace and mining industries were indifferent to it until its dimensions became clearer in the late 1970s. By early 1980, however, the opposition had managed to enlist such allies as Senators Frank Church and Jacob Javits and, with their aid, had persuaded President Carter not to endorse the treaty.

As for Antarctica, a much more immediate concern, the treaty now governing the area mainly concerns scientific matters and explicitly does not override any claims made by any of the twelve contracting parties—the United States, the Soviet Union, and ten other developed nations. Recently, however, the Group of 77 and other third world nations, which are not parties to the existing treaty, have been pushing to remake it into an instrument for internationalizing the entire continent. That would mean declaring that the Antarctic is the common heritage of mankind and setting up some plan to share the mineral wealth extracted.

The Transfer of Technology

To many in the third world, the key to rapid economic gains for their countries lies in the internationally regulated transfer of technology from the developed world. In their minds —and in those of many in the international regulatory bureaucracy—traditional foreign aid is demeaning and ineffective. Moreover, they believe, ordinary arrangements for acquiring technology from multinational corporations are inadequate because of fundamental inequalities in bargaining strength.

UNCTAD has provided a sympathetic forum for efforts to redress that imbalance. From 1973 on, many in this organization have argued that its goal of promoting third world development could best be served through the adoption of a universal technology transfer code, whose details would be implemented through national legislation. The Group of 77 made the first move in 1975, submitting a draft code so one-sided that the developed nations countered with their own draft a year later. About the same time, the Soviet bloc weighed in with a third proposal. To UNCTAD's secretariat fell the unenviable task of putting together a tolerable compromise.

The likelihood of success seems slim. The Group of 77 draft draws heavily on the provisions of regional codes (especially the Andean Pact, encompassing five Latin American nations) and national laws (such as Brazil's and Mexico's) that impose severe limitations upon those who would engage in the business of transferring technology—a term, incidentally, that the document does not adequately define. It requires that foreign multinational corporations sell, rather than license, the technology they would use in a particular country. Moreover, reflecting the Group of 77's deep-seated bias toward regulation, this would have to be done at prices *no higher* than current world levels and on contractual terms to be established largely by the recipient country.

Scarcely less onerous are the requirements of the Group of 77's draft that multinationals wishing to market their technology guarantee its "appropriateness" for the local end user. Along with conventional warranties, the foreign company would have to ensure minimum production levels that could be reached through use of their technology, notwithstanding the directive that local personnel be used in relevant consulting, engineering, and servicing work. Where these local specialists would come from is unclear, even considering all the training that the multinationals would be ordered to provide.

Nor is that all. The Group of 77 draft ignores the many established neutral forums for resolving international disputes and instead relies exclusively on the courts of the receiving nation. And even though the government of the receiving nation would be heavily involved in the technology transfer, the transferor's gov-

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ernment would not be allowed to intervene on behalf of its citizens if their property were unjustly taken.

A technology transfer code is not likely to move forward soon. As the issues were being focused in the late 1970s, the Carter administration began to express reservations, and the Reagan administration is even more doubtful. Lengthy efforts in the spring of 1981 failed to result in an acceptable compromise.

Multinational Corporate Conduct

Stymied on technology transfer, UNCTAD has made some progress with its Code on Restrictive Business Practices, which the UN General Assembly adopted in 1980 in spite of ongoing efforts by the OECD to reach consensual standards covering such concerns. This code requires multinationals to "unbundle" their technology and know-how, no matter how much technical and commercial sense it may make to offer them as a package. A second target of the code is restrictions imposed by technology owners on local recipients of technology as to acceptable sources for goods and raw materials, production goals, the use of competing and complementary technology, the sale of competing products, the local retransfer of the technology in question, and local research and development. Also prohibited are requirements that the recipients of the technology in question use personnel recommended by the technology owner, grant back to the owner all improvements made in the technology, and buy further improvements and inventions from the owner.

Lest UNCTAD be the only game in town regulating the activities of multinationals, the UN Economic and Social Council set out in 1974 to formulate its own code to govern relations between multinational corporations and interested (home and host) governments. Acting on the mandate provided by the New International Economic Order, the council established a forty-eight member Commission on Transnational Corporations which, through its Intergovernmental Working Group, has drafted a number of working papers and the outline of a code. Not surprisingly, given that the Western democracies are the home base of almost all multinationals but have only ten members on the commission, and given also that the commission made no provision for serious participation by business representatives, the working papers call for one more international regulatory regime heavily slanted against free market principles. To start with, the scheme would be directed only at private multinational corporations, even though some fairly powerful state-owned enterprises are engaged in foreign commerce. As for specific prohibitions, the working papers propose to require that multinationals submit, for host government approval, not only all technical agreements but also the underlying technical data. Should this proposal prevail, host governments would be free to exploit that information in certain contexts —becoming, in effect, third-party beneficiaries of technology transfers.

Nor are technical agreements and technology the only information that multinationals would have to communicate to host governments. Responding to third world nations' claims that the lack of hard information about multinationals makes oversight of their activities difficult, the working papers would require multinationals to disgorge volumes of business information at the request of the host government, including data on worldwide and intracompany pricing, marketing practices and performance, taxation, research and development goals, and the like. And the host government would be permitted to make much of this information available to private parties.

The working papers are also troublesome in their treatment of the binding effect of contractual agreements entered into by multinationals. They provide that such contracts may be renegotiated in connection with national development plans and regional integration arrangements. And they would permit host governments in certain situations to restrict the rights of multinationals to repatriate profits and other funds, notwithstanding contractual niceties or local law.

The Liner Code

UNCTAD has had even greater success with its code on world shipping, the Code of Conduct for Liner Conferences. This code has already been ratified by more than fifty countries, representing some four-fifths of the 25 percent of world tonnage required for adoption. Ratifica-

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tion by the European Economic Community, postponed last May at the request of the United States but now imminent, will bring it into effect.

The Liner Code is an effort to promote the maritime industries of developing nations by mechanically allocating the shipping tonnage of ratifying nations. Under the most widely suggested formula, 80 percent of the cargoes in bilateral trade would be divided equally between the ships of the two trading partners, regardless of their ability to offer competitive rates and service. Only 20 percent would be left for third party ships. The pact contemplates the eventual abolition of "flags of convenience," such as those of Liberia and Panama, which currently are a chief source of maritime competion.

The 145-article code also limits rate increases to one every fifteen months and dictates that disputes be settled by a mandatory conciliation process, rather than pursuant to national law or practice, regardless of the disputants' wishes. In addition, it conflicts with U.S. customs and laws in a variety of ways. For example, it runs counter to the long-standing U.S. practice of maintaining open liner conferences, and it fails to accommodate U.S. laws which require that government and government-financed (Export-Import Bank) shipments be carried by U.S. flagships.

It is striking that third world governments should expect to benefit by such forced market-sharing. Nobody is going to give them any ships for free; they will have to either plow their scarce currency reserves into the highly capital-intensive shipping business, or circumvent the rule by in effect selling their flag rights to foreign operators. Any money they succeed in raising by the latter means will be taken directly from, and will serve as a hindrance to, their foreign trade, much like a tariff applying to both imports and exports.

Exports and Imports

Although the new international regulators take restrictionist positions on the goods and services imported from the developed nations, they would require those same nations to open their markets wide to the export products of third world countries. It is an exercise in self-serving inconsistency, where the developed nations' duty to heed the special imperatives of third world growth—as seen in that world—becomes the overriding principle.

It is an exercise in self-serving inconsistency, where the developed nations' duty to heed the special imperatives of third world growth—as seen in that world—becomes the overriding principle.

Textiles, apparel, footwear, leather products, and steel are the third-world exports most often at issue. Of late, much attention has focused on textiles, principally because the so-called Multifiber Agreement (Arrangement Regarding International Trade in Textiles) expires on December 31, 1981, unless it is renewed. Established in 1973, this agreement was an effort to increase third world textile exports to the developed world in such a way as to avoid market disruptions large enough to lead the United States, Japan, and the Western European countries to raise protectionist barriers. As the renewal date nears, the third world, together with the European Economic Community, is arguing that the United States should again accept the agreement's regulatory regime (which requires increases in U.S. textile quotas of 6 percent a year), rather than adopt the likely alternative of linking the quota to U.S. market growth (which is more like 1 to 3 percent a year).

Even while pushing such schemes, the less developed nations argue that, because they have trouble competing in the developed world, they should be exempt from the basic international trade standards that most of the world's nations have accepted through GATT (the General Agreement on Tariffs and Trade). GATT is a voluntary mechanism established after World War II to sponsor multilateral negotiations for reducing trade barriers. During the Tokyo Round of the GATT multilateral trade negotiations (1973 to 1979), the major trading nations agreed on rules designed to deter dumping (export sales at prices below home market prices or, in some cases, production costs) and unlawful government subsidization (as defined in the agreement). Although many less developed countries participated in these negotiations and

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although the final agreements give such countries special treatment until they graduate into full membership in the world trading community, most of the third world joined in the denunciation of the entire Tokyo Round delivered at the 1979 UNCTAD session in Manila. As a result, few third world nations have signed the Tokyo Round agreements, though their failure to do so deprives them of GATT's benefits.

New proposals applying to pharmaceutical and health products offer additional examples of third world "regulationism." During the past six years no fewer than four different UN entities—UNCTAD, the UN Center for Transnational Corporations, the United Nations Industrial Development Organization (UNIDO), and the World Health Organization—have involved themselves with the pharmaceutical industry, necessitating the creation of a special UN task force just to coordinate their activities. So far, the products of this regulatory effort include the adoption by WHO of a worldwide ban on the advertising of infant formula (even though the industry had already imposed effective standards on itself); the development by UNIDO's staff of proposals to redistribute the wealth of the pharmaceutical industry by limiting royalties and prices and by giving third world governments the know-how and (where necessary) the rights to enable them to produce certain basic drugs; and the development by WHO's staff of plans for the international regulation of drug quality. The latter proposal, news of which has only recently come to light, would create a supranational regulatory agency to pass on drug quality and to bar, if it saw fit, the marketing of pharmaceuticals already approved by competent national authorities, such as the FDA. This "international FDA" would support the substantial bureaucracy proposed for it by exacting large fees from pharmaceutical firms. Under the provisions of the staff draft, this agency would not be compelled to give adequate protection to proprietary data submitted to it in confidence and, in some instances, would even be able to enforce its decisions by threatening to publicize the data "in the general interest."

[WHO's staff proposal] would create a supranational regulatory agency to pass on drug quality and to bar . . . the marketing of pharmaceuticals already approved by competent national authorities. . . .

The New World Information Order

Running parallel to the New International Economic Order and perceived by many in the third world as a vital part of it is yet another "new order"—the so-called New World Information Order. Its stated objective of promoting the free movement of information across national borders is certainly appealing. As defined by much of the third world, however, with some prompting from the sidelines by the Soviet Union, the New World Information Order poses a regulatory threat of substantial magnitude to the accepted norms of free journalism, the free flow of ideas, and the free exchange of data.

The basic dimensions of this scheme have been crystallizing since the 1976 UN Educational, Scientific, and Cultural Organization (UNESCO) conference in Nairobi. At that conference, the Soviet Union sought final acceptance of its four-year-old proposal for restricting the role of foreign (that is, independent, Western) news agencies in the third world. The initiative failed. But it attracted enough support to cause the conference to appoint a sixteen-member commission, headed by former Irish foreign minister and Amnesty International official Sean MacBride, to study ways of "achieving a freer and more balanced flow of information."

The MacBride commission gave very short shrift to press freedom. It focused its attention, instead, on what it called the concentration of press power in the hands of a limited number of "transnational" news organizations headquartered in the West, including the Associated Press, the United Press International, Agence France-Presse, and Reuters. While rejecting the proposals of its more radical members to "correct imbalances" in the Western press by penalizing errant journalists, it did adopt and forward to UNESCO eighty-two recommendations for reshaping the manner in which news is gathered and transmitted.

Many of these recommendations were unprecedented. The commission urged, for ex-

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ample, that thought be given to subjecting journalists to an internationally developed and monitored code of ethics and to providing them with some (as yet unspecified) form of international "protection." Journalists who practice their craft in nations having some semblance of a free press—all Western democracies, a number of Latin American countries, Japan, and a handful of other states—have opposed these ideas as thinly veiled limitations on a free working press. The same is true of the recommendations for opening the media (by regulation) to "previously unheard" groups and for controlling relations between international news organizations and local governments. On the former point, the commission suggested studying whether it would be feasible to establish an international broadcasting arm for UNESCO and to create an international right of reply—giving governments, groups, or individuals who claim to have been misrepresented in the news an opportunity to respond. On relations between the media and local governments, the commission's position is best summarized in its call for "effective legal measures designed to circumscribe the action of transnationals [news organizations] by requiring them to comply with specific criteria and conditions defined by national development policy [especially in the developing world]."

Suddenly awakened to the threat posed by the MacBride commission's recommendations, the United States and its allies managed at the 1980 UNESCO meetings in Belgrade to defer a budget resolution that would have funded work on a code of ethics for journalists and a definition (to be applied to the major news organizations) of what constitutes "socially responsible communication"—as well as one other proposal for global regulation, an international advertising code. It was not possible, however, to prevent the UNESCO secretariat from formulating, in the vague terms described above, an outline for the New World Information Order.

To date, the principal battles in this area have been over news. But growing numbers of third world countries are now seeking, in UNESCO and in other forums, to extend the effort to other aspects of information gathering and transmission, particularly computers and satellites. Their representatives have denounced multinational businesses for what they characterize as a one-way flow of the business and other data they generate from the third world to the developed world. Viewing information as a key to power, they have argued for both international and national regulation of that data flow—and without the safeguards for privacy built into the consensual codes on which OECD and the Council of Europe are at work. As a third world representative said at Belgrade, every nation has the "right . . . to develop national sovereignty and cultural identity by regulating transnational corporations."

Of Dubious Benefit for All

This new, highly politicized scheme of international regulation is replete with problems, for both developed and less developed nations and for their citizens as well.

For the United States and other developed nations, the proposals not only threaten immediate commercial, economic, and political interests but also conflict with the principles of free enterprise and a free press that are the foundation of the very affluence that the third world is seeking to share. At their boldest, the international regulators seek mandatory redistribution of wealth from the developed world. The space treaty and draft Law of the Sea treaty would bring it about by obligating multinationals to surrender part of the mineral wealth they extract. The proposals on technology transfer and multinational conduct would do it less directly by allowing host governments to cast and recast contractual terms involving foreign businesses, and the Liner Code and Multifiber Agreement would create artificial commercial opportunities for third world enterprises. Finally, striking at the free movement of information, many of the proposed codes urge the yielding up of data generated by the developed world and the closing down (or the shaping) of that produced by the third world.

Bad as much of this new international regulation might be for the developed world, it would be far more harmful to the developing world itself. By ignoring the realities of capital formation and economic incentives, it would greatly impede the accumulation and flow of capital and resources that are the true prerequisites to developing both the technology and the economic growth sought by the less developed nations. No reasonable person would

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deny that the third world, with its abundance of natural resources and its populous markets, is important to Western business. But the fact is that, by and large, the less developed countries are by no means as vital as ideologues believe them to be. To use an example noted by Raymond Waldmann, the Commerce Department's assistant secretary for international economic policy, more than 90 percent of all technology transfers by private enterprises occur outside the less developed countries. It is folly to assume that the multinationals responsible for these transfers will freely divulge valuable data just to hang on to the little business and less profit that so many of these countries represent. What they are far more likely to do is refuse to undertake new technology transfers to, and investments in, the nations involved—leaving those nations the poorer for their futile regulatory effort.

But even if some in the multinational business community were to involve themselves in the third world under such terms, there is serious doubt that the recipient countries are equipped to administer the new controls they desire. Notwithstanding major efforts at training a new managerial class, most of these countries already are woefully short of the professional personnel needed to collect, evaluate, and act upon—in short, to use and regulate—technical and business data. Do they really want to devote their all too scarce educational resources to the task of training regulators?

Likewise, if businesses and news organizations cannot gather data freely in the third world, the developed nations will undoubtedly suffer, since they will lose access to accurate political, cultural, and economic information from that part of the world. But the less developed countries will lose even more. Not only will their concerns be less intelligible to the rest of the world, but they will lose what are, in many instances, the most reliable and forthright sources of information about themselves and about each other.

Looking Forward

For all the flaws of these international regulatory schemes, it is neither responsible nor practicle to ignore the circumstances that have given them birth. The hard fact is that the gap between rich and poor nations continues to widen—that, by the turn of the century, as many as 850 million people may be living in abject poverty.

Still, handouts are not the answer. Even if the United States and its allies were capable of sustaining a quarter of the world's populace indefinitely, wealth transfers have shown themselves to be all but useless in helping the masses of the less developed countries break out of poverty. Nor does the answer lie in international regulation. Much of that effort is just as demeaning and counterproductive as traditional foreign aid. Even worse, it would sap the vitality of the very economic forces and entities that could, given the chance, show the third world how to help itself.

Insofar as there is an answer, it lies in more decentralization and more freedom rather than in tighter regulatory fetters, whether of the national or transnational variety. The sorry economic performance of the world's command-and-control societies is itself the most convincing witness for the wealth-creating power of free institutions. Compare, for example, such pairs of nations as East Germany and West Germany, Burma and Singapore, Tanzania and Kenya—and, for that matter, the Soviet Union and the United States. In each instance, the country whose politics and economics are freer has grown far faster. What an irony it is that, in the face of this record, the international regulators have turned to the model that has failed—a model that can only spread the stagnation and dependence now gripping parts of the third world.

By the time these words are read, the basic issues underlying the new international regulation will have been aired at the Cancun Conference, held in Mexico on October 22-23. There, the leaders of the third world nations and others will have urged the United States to follow the course of international wealth sharing—Global Negotiations under UN auspices looking toward the creation of the New International Economic Order. There, also, President Reagan will have pressed the third world to focus instead on free market solutions—on combining cooperative international approaches with the use of positive incentives in order to promote true economic development. In many ways, then, to the extent that the proposal for Global Negotiations flourishes in the aftermath of Cancun, so will international regulation. ■

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Nursing the Railroads Back to Health

Mark M. Levin and
Bruce N. Stram

THE SORRY STATE of the U.S. railroad industry is well illustrated by a recent press release from its trade group, the Association of American Railroads. The release proudly proclaimed that the industry's return on investment had climbed to 4.3 percent in 1980—the highest level in twenty-five years. Such a return, which would have been barely acceptable back in 1955, is frighteningly depressed in today's inflationary conditions. Yet the AAR correctly observed that it was much better than the 2.9 percent return earned in 1979. Clearly, our once mighty railroads are now the poor relations of American industry. And the main causes of their decline are obvious enough, too: heavy-handed, irrational regulation and intense competition from other modes of transport.

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The basic patterns of railroad regulation, established almost a century ago in wholly different market conditions, are simply obsolete. Their premise is that railroads have a collective monopoly, or near-monopoly, in land transport and therefore, unless restrained by regulation, can earn "monopoly" (or "excessive") profits. That condition disappeared long ago, if indeed it ever existed. Nearly every sphere of rail freight service now faces intense competition, often from modes that evolved well after the regulatory system was conceived; and passenger service, once a major source of rail revenues, has lost out to airlines, buses, and automobiles. Despite all this, the Interstate Commerce Commission (ICC) still treats the railroads as monopolies, hobbling them so effectively that their very survival is in question.

We offer here a proposal for nursing the industry back to health and for testing the need for continued regulation. Our scheme allows for the reimposition of a regulatory system, though a more rational one, in the unlikely event that should prove necessary.

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Legislative Efforts to Ease the Railroads' Plight

In the past decade Congress spent an inordinate amount of time on the plight of the railroad industry. Its efforts yielded several lengthy and often murky pieces of legislation designed to improve railroad profitability—the 3R Act of 1973, the 4R Act of 1976, and the Staggers Rail Act of 1980. The simple fact of sustained and grossly subnormal rail profits should have led Congress, in the course of these prolonged deliberations, to ask whether the monopoly rationale for regulation was still valid. Although the Department of Transportation attempted to force this issue by drafting a broad-ranging deregulation bill in 1978, political pressures quickly stymied its effort.

Nevertheless, the recent legislation has solved some serious problems. The railroads' freedom to adjust prices without interference was significantly enlarged by a provision that limits regulatory scrutiny to rates in the upper third of the rate structure. Indexing of existing rates to keep pace with inflation is now automatic. Railroads can now promptly stem their losses on money-losing, little-used branch lines, either by taking advantage of accelerated abandonment procedures or by imposing rate surcharges with minimal regulatory interference. Contracts between shippers and railroads are permitted for the first time and are virtually free of regulation.

Perhaps most important of all, the legislation directs the ICC to allow the railroads sufficient rate freedom to earn "adequate revenues" under "honest, economical and efficient management." Inclusion of such a fundamental requirement hardly seems significant or even necessary and, in fact, would appear to be constitutionally required. Its importance becomes apparent only when it is recognized that for twenty-five years the ICC persistently slashed rate increases, even though the railroad industry failed to earn normal profits in any one of those years.

While Congress's "revenue adequacy" directive is a major milestone in the history of railroad regulation, its practical effect may be in doubt. In the 1980 act, Congress left to the ICC the difficult job of defining precisely what level of rail revenues is "adequate" and of formulating specific maximum-rate policies to achieve this somewhat vague objective. Given the ICC's record in rate regulation, this was a risky decision. Congress should have learned its lesson in 1976 when the objectives of the 4R Act were scuttled by a commission determined to perpetuate the status quo.

The Failure of ICC Regulation

It is astounding, yet true, that in its almost 100-year existence the ICC has failed to develop any coherent theory of rate regulation, let alone one based on the principal rationale for economic regulation—restraint of monopolistic or excessively high rates of return. Other regulatory agencies—the Federal Communications Commission, Civil Aeronautics Board, Federal Energy Regulatory Commission, and the state public utility commissions—and even the ICC itself in the motor carrier area have pursued rate of return regulation as the most logical approach to rate regulation. But in the case of railroads, the ICC has avoided any such approach. It is not that the commission has formulated some alternative theory of rate regulation for the industry; rather, its rate policies have simply been arbitrary and capricious. A typical commission decision consists of a summary of the facts, a string of legal citations, an almost religious incantation of various statutory terms and other code words that mean wildly different things to different people (including different ICC commissioners), a calculation of variable and fully allocated costs through the use of an antiquated costing system that everybody (including the ICC) recognizes as inaccurate, and finally the ordering paragraph. Even seasoned observers do no better than fifty-fifty at predicting how ICC cases will come out.

Recently, however, responding to the new revenue adequacy directive, the ICC has attempted to bring some measure of rationality to its policies. In *Ex Parte* No. 393, *Determination of Railroad Revenue Adequacy* (1981), the commission set 11.7 percent as an "adequate" rate of return on the original investment base. Since none of the major railroads did in fact enjoy that high a return, all of them were declared to be "revenue inadequate" and thus entitled to an added measure of rate freedom. Most important, the ICC's decision recognized

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that railroads, in order to survive in the long run without governmental assistance, must earn a rate of return high enough to compete effectively in the capital markets. While such a holding might seem elementary to an outside observer, one railroad executive has called it "the industry's *Brown* v. *Board of Education.*"

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Translated into dollars, the ICC's decision means that in 1981, the railroads must net at least $2 billion more than their 1980 earnings of $1.3 billion if they are to achieve "revenue adequacy." While this is no small increase, the amount needed for any real adequacy will be substantially larger, because the 11.7 percent figure does not reflect the much higher interest rates of 1980 and 1981. A reasonable estimate is that rail revenues are, in the aggregate, 10 percent or $3 billion too low—in other words, that much below the level that will ensure continued service in the long run without government subsidy.

It might seem that a straightforward 10 percent increase in all rail rates would solve the problem. But, if it were so simple, even the ICC might have remedied matters by now. In fact, there is so much competition for so many rail shipments that a 10 percent across-the-board hike would actually reduce railroad traffic and revenues. Moreover, traffic would decline somewhat even for those shipments where a rate hike would increase net revenues. In short, to earn the needed additional revenue, rate hikes must be selective and must substantially exceed 10 percent in real terms for many shipments.

The ICC's decision in *Ex Parte* No. 393 was a crucial first step toward developing a coherent rate policy. But what the commission gives with one hand, it frequently takes away with the other. In subsequent coal rate cases and in *Ex Parte* No. 347, *Nationwide Standards for Coal Rates* (1981), it has reverted to regulating rates one at a time, with no consistent standards. Specifically, it has reasserted its view that rates can be deemed "unreasonable" if they exceed specified percentages of fully allocated cost, or variable cost, or some other accounting convention, without reference to the level of rates charged on other commodities.*

The current ICC rate policy, insofar as any consistency can be found, appears to be that rates are "reasonable" if they do not exceed the fully allocated cost of the transportation, with fixed costs allocated by the "ton/ton mile" formula—that is, according to the weight of the shipment and the distance it travels. This is a departure from the previously used "ratio" method, where fixed cost is a function of the variable cost of a particular service. Under that method, the commission looked at newly filed coal rates and found them reasonable if they did not exceed 107 percent of fully allocated costs—the much ridiculed "7 percent solution," concocted as a political compromise and not as a result of any economic analysis. It did not, however, police existing rates on other traffic, leaving them to range all over the map, from under variable cost to four and five times variable cost. These almost randomly regulated rates applied then, and still apply, to the vast majority of all rail traffic—a reflection of decades of crazy-quilt regulation.

Elasticity Pricing

The switch from the 7 percent solution to the ton/ton mile solution has the effect of allocating a higher share of fixed costs to commodities such as coal which, because of their high

*Some definitions may be useful. "Variable costs" are those costs that vary in the long run with the level of service provided, according to ICC costing formulas. The ICC has determined that 78 percent of total rail costs are "variable" and 22 percent are "fixed." "Fixed costs" must also be recovered even though they cannot be associated with the provision of any particular transportation service. The sum of the variable costs of a transportation service and the allocated fixed costs equals "fully allocated cost." Fully allocated cost has in recent times included the current cost of capital.

"Incremental cost" is an economic term, not an accounting term. It is the additional cost a railroad incurs in providing an additional unit of service. "Long run incremental cost" should approximate "variable cost" assuming the commission's costing methodology produces reliable results, which it does not. Similarly, a more technically correct economic term for fixed costs is "common costs" or "unattributable costs."

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density (because they weigh more per unit of cubic capacity than most other goods), frequently do not have alternatives to rail transport. Framers of the ton/ton mile proposal hoped that the switch would accomplish two things: (1) bring rate relationships more into line with the relative demand elasticities of the shippers and (2) bring railroad revenue up to adequate levels by allocating a larger share of fixed costs to price-inelastic shippers. Elasticity in this context is a shipper's willingness to substitute alternatives for the services of a particular railroad that has raised its price relative to the price of alternatives. Shippers who will shift when a price increase is small are relatively price-elastic; shippers who will find substitutes only when price changes are large are relatively price-inelastic.

For reasons of economic efficiency, fixed costs should be allocated on the basis of relative demand elasticities. Shippers with relatively inelastic demand should pay a higher share of fixed costs than price-elastic shippers. The logic of this is fairly simple: shippers with greater elasticity of demand by definition have more transport alternatives than shippers with lesser elasticity of demand and will choose those alternatives if the rate charged by the rail carrier is higher than that charged by the competition. As long as the rail rate charged to the price-elastic shipper is higher than the incremental cost of the service, the rate is contributing to rail overhead (fixed costs). Thus all shippers benefit when price-elastic shippers elect to ship by rail. This is true because the pool of fixed costs by definition is constant in size; to the extent that price-elastic shippers pick up any of the burden, the remaining burden will be lower, and thus price-inelastic shippers can be charged lower rates. Consequently, so-called differential pricing, tied to demand factors, benefits all shippers, even though it seems unfair that some shippers should have to pay rates representing higher multiples of cost than other shippers.

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Ramsey Pricing

The particular formula for elasticity pricing that theoretically maximizes economic efficiency is called Ramsey pricing. This approach to rate regulation was first expounded in a classic paper by a British mathematician and economist, Frank Ramsey. Now, in *Ex Parte* No. 347, the railroads have urged the ICC to adopt Ramsey pricing principles in adjudicating the reasonableness of rate levels; the ICC has yet to rule on the issue.

Under Ramsey pricing, each shipper is charged a rate equal to the incremental cost of the service it receives, plus a share of the railroad's fixed costs inversely proportional to the shipper's elasticity of demand for service (calculated according to a complicated statistical formula). Hence coal shippers who could easily use water transportation would pay a lower rate than coal shippers whose only choice is rail transport.

In competitive industries, the profit-maximizing price is the same as the economically efficient price. If transportation markets are competitive and railroads can earn no more than a market rate of return under unrestricted pricing, then the rate schedule they adopt voluntarily will be a Ramsey scheme. Because increases above these rates would cause traffic to decline enough to lower overall profit, a railroad will limit its rates to those levels voluntarily. If a carrier is capable of earning excess profits in the absence of regulation, however, Ramsey pricing regulation would hold all rates below the profit-maximizing level in proportion to the shipper's price elasticity.

In calculating incremental costs and the pool of fixed costs under a Ramsey pricing system, only a competitive rate of return on capital is permitted. Further, should a carrier charge less than the Ramsey price for the service either by mistake or by design, the resulting shortfall cannot be recovered by charging other shippers more than the Ramsey price. These two important features of Ramsey pricing allow the carrier a return equal at most to the cost of capital, and prevent cross-subsidization.

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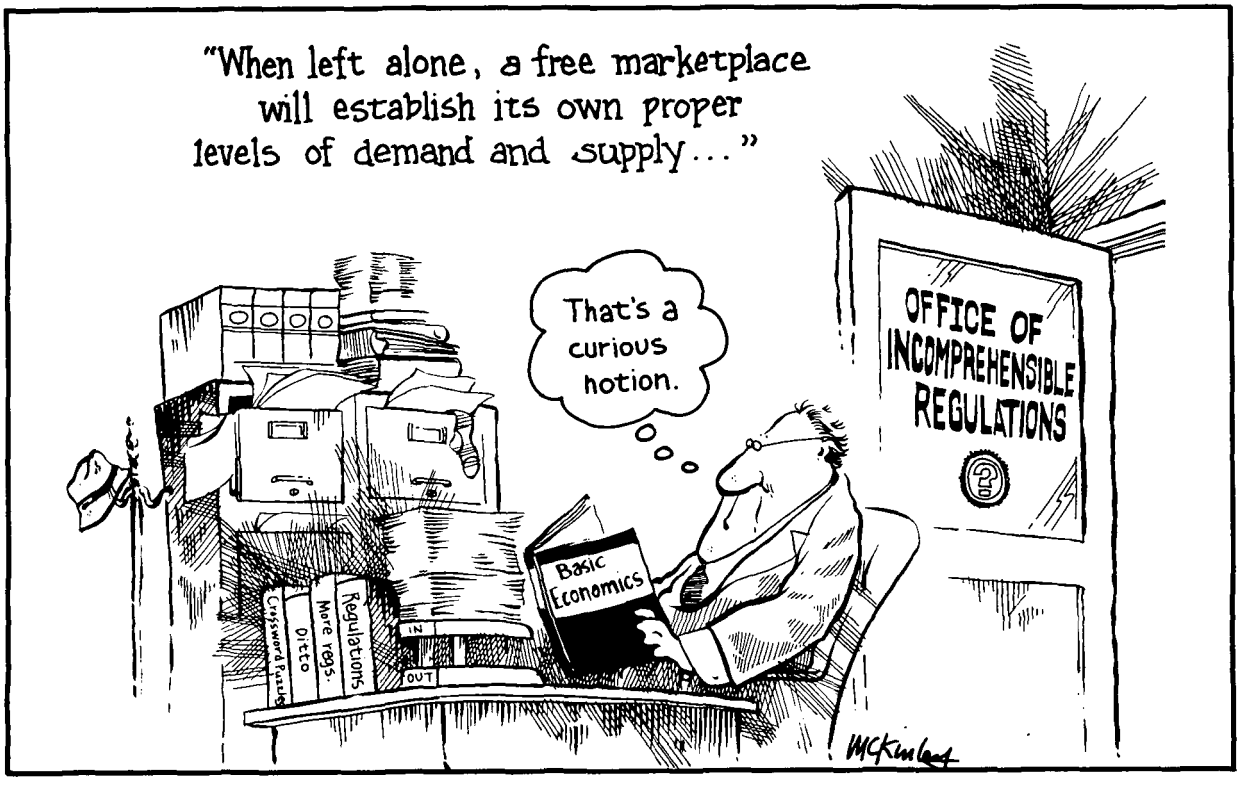
If unrestrained railroads are in fact capable of earning excessive profits, all shippers would receive a lower rate under Ramsey pricing than they would under complete deregulation; if not, shippers would be charged what the market will bear.

Ramsey pricing would present no administrative problem at all in the latter case, since complete deregulation would be appropriate. But in the former case, Ramsey pricing would require calculating relative elasticities for every relevant shipper or group of shippers that uses a railroad, once that railroad had achieved adequate revenues. That is all but impossible to do with any degree of accuracy.

The ton/ton mile solution was intended to be a proxy for these exceedingly difficult calculations. Unfortunately, the solution is seriously flawed in this regard: In the West it would allocate a higher share of fixed costs to relatively inelastic coal shippers who use rail service, thereby raising some newly filed western coal rates. But in the East and South, it would actually call for lower rates, primarily because capricious rate regulation had resulted in high allocations of fixed costs there. The railroads claim, with substantial evidence, that consistent application of the ton/ton mile solution to all rates would reduce their total revenues by over $1 billion from current levels. Thus the ICC proposal runs counter to its framers' intended goal and, if implemented, would actually exacerbate the railroads' revenue problem. That the 7 percent solution applied to the entire rate structure would cause even greater devastation is little solace.

We must conclude from the commission's unfortunate experiment with the ton/ton mile solution that there is no formula based on accounting conventions that will efficiently produce adequate revenue levels when applied to all rates. This is true because there is no systematic correlation between demand considerations and any cost accounting convention. The reasonableness of individual rates can be judged only by reference to all of the other rates charged by a carrier and the effect that the resulting rate structure has on the carrier's bottom line. No matter how high an individual rate may climb as a multiple of variable cost, a railroad simply will not be able to raise the capital it needs in the long run unless its net rate of return is competitive. Consequently, there is no magic in "fully allocated cost" or "variable cost" percentages no matter how they are calculated. All that such percentages reveal is that



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certain rates contribute more to fixed costs than other rates.

A Modest Proposal

To overcome these difficulties, we offer the following modest proposal: hold all pending and future rate cases against a carrier in abeyance until that carrier's earnings exceed the revenue adequacy level, except for cases where the carrier seeks an increase in any one year of more than 6 percent (after adjustment for inflation). In our view, this is the best course now available to the commission that (1) is consistent with sound economic principles, (2) treats shippers fairly, (3) allows railroads the chance to earn adequate revenues, (4) is legally sustainable, and (5) is administratively possible.

Let us examine the reasoning for this proposal, beginning with its insistence on gradual rate increases. Given that railroad industry earnings are so depressed, why should carriers not be permitted to raise their rates as fast as possible to achieve revenue adequacy? The main reason is that shippers are more likely to tolerate gradual than abrupt change and that a degree of shipper toleration is needed to keep political pressures directed against the program from becoming irresistible.

Economic principles also counsel gradualness. Coal and chemical shippers honestly fear that they will have to pay the whole tab if the railroads are given unlimited freedom to raise rates until revenues reach an adequate level. That is, they assume that rail managers will take the easy road and simply pile all of the increases needed to achieve a competitive rate of return on a few types of price-inelastic shippers. Our proposal is designed to allay that fear. Given the current rates of return of most major carriers, real rate increases of 6 percent imposed only on coal and chemical shipments would be insufficient, by a wide margin, to yield adequate revenues for several years, if ever. By limiting rate increases to 6 percent a year, our program would create strong incentives for carriers to adjust all of their rates in order to maximize return as well as to reduce costs wherever possible. Both of these courses would improve the bottom line during the transition period.

The choice of 6 percent as opposed to some other percentage is certainly arbitrary, but it has an advantage legally: Congress has sanctioned it. The Staggers Rail Act created a 6 percent zone within which rate adjustments may not be challenged until the rate is in effect, and even then the challenger must demonstrate that the rate is unreasonable. While a court would most likely strike down a 6 percent zone if the commission picked the number out of the air, Congress is free to be arbitrary. Here then is a tool the commission may use to bring rationality to the rate structure.

Another important legal feature of the proposal is that the enormous backlog of rate complaints currently pending at the commission would be held in abeyance rather than simply dismissed. The Staggers Rail Act stripped the commission of jurisdiction over all existing rates (the base rate plus adjustments for inflation) except for those challenged in complaints filed by April 1, 1981. Faced with this speak-now-or-forever-hold-your-peace provision, shippers of every conceivable stripe naturally filed complaints—more than 800 of them. Should these complaints now be dismissed, the challenged rates would be freed from regulation as well. While it is extremely unlikely, in our view, that any of those rates would be reduced under a rational system of rate regulation based on elasticity principles, this assertion cannot be proved until a rate structure evolves that is capable of producing revenue adequacy. As long as any question remains, the door should be kept open, so that the shipper whose case is held in abeyance has the right to demonstrate unreasonableness and win a prospective rate reduction later.

It is important to emphasize that the shipper would be permitted such reductions only if the carrier were earning more than "adequate" revenues. Because no carrier has yet reached that level, there is no economically rational basis for finding any existing rate unreasonable today. If railroads earn inadequate revenues because regulation has forced some rates below the "correct" level, the remaining shippers on the railroad should be charged more than the correct level to make up the shortfall. This is necessary if the railroad is to survive. Assuming regulation is the cause of the railroads' plight, we have the worst of all possible worlds today: some rates are held below correct levels, while others are not permitted to rise sufficiently above those levels to make

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up the shortfall. While it cannot be rationally determined which existing rates (if any) are too high today, such an argument can be made if and when railroad earnings rise above revenue adequacy. At that time prospective decreases in those rates that are today above the correct level should be ordered.

The Competitive Environment

In our view, the most attractive feature of our proposal is that it would inevitably lead the ICC to question the rationale for its very existence. And the ICC, to its surprise, would probably find that, with competition preventing railroads from earning excess profits, rate regulation is not needed.

[O]ur proposal . . . would inevitably lead the ICC to question the rationale for its very existence. And the ICC, to its surprise, would probably find that, with competition preventing railroads from earning excess profits, rate regulation is not needed.

Railroads clearly face intense competition for nearly all of the services they provide—from trucks, pipelines, barges, ocean and lake carriers, as well as from other railroads capable of moving commodities between the same two points. With the abolition of antitrust immunity for collective ratemaking (legalized price-fixing) currently scheduled for 1982, rate competition among the railroads is certain to intensify. Source competition further limits a rail carrier's ability to charge excessive rates: purchasers can often obtain a product from several origins served by different carriers and modes, while many producers can ship by different carriers and modes to a variety of destinations.

None of this is to deny that, in many instances, railroads have market power—that is, they can charge rates that exceed the incremental cost of service. Not only do they have such power but its exercise, at least to a degree, is absolutely essential if they are to survive. Railroads have substantial fixed costs common to a variety of activities and some economies of density. This means that their incremental cost of service is less than their average cost of service. Consequently, if all their services were priced purely competitively—at incremental cost—the railroads would be unable to cover their total costs and would, after cannibalizing their assets, cease to exist. Each of the services provided by a railroad must be priced with an eye on the competition, but in the aggregate they must be priced sufficiently above incremental cost to recover total costs (including a return on investment equal to the cost of capital).

Given the competitive conditions, it is by no means clear that the ICC need continue regulating rail rates indefinitely. Its only legitimate regulatory mission is to restrain excessive railroad profits over the long run—and market competition may already provide this restraint. Our scheme should be viewed as a controlled experiment designed to determine whether the market will in fact do that job, and thus whether regulation should be ended. Equally important, it keeps open the option of imposing rational restraints, should that prove necessary. As things stand now, any economic benefit that accrues to society from current ICC regulation is purely fortuitous.

A Rough Surrogate

Our proposal is really a rough surrogate for Ramsey pricing, one that would make its application administratively possible, should the carriers' earnings begin to exceed the adequacy level. The rate structure that would result from implementing the proposal would closely resemble a Ramsey structure that had been accurately measured with the requisite mathematical precision. Shippers with more inelastic demand, as measured by railroad pricing officers, would systematically be subject to greater increases and hence would pay a higher share of fixed costs, cross-subsidization would be minimized, and carriers would increase their net revenues at a relatively quick pace.

With the adoption of the proposal, railroad pricing officers would aggressively seek to increase rates for price-inelastic shippers by the full 6 percent, while being more cautious in their pricing where shippers had alternative transport or faced strong competition in the sale of their product. Furthermore, they would have every incentive to ensure that all rates

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were above incremental cost. Each year railroads would take the full 6 percent increase on fewer and fewer rates—as profit incentives led them to limit their increases in recognition of the increasing attractiveness of alternatives to shippers. Our scheme thus offers the commission a means for relying on the profit incentive, which governs most of our economy, to establish a rate structure that permits adequate revenues and is reasonably efficient.

Such a structure, in addition, should provide extremely useful data for figuring Ramsey elasticities in the event that regulation of the rate structure proved to be necessary in the long term. Should rail revenues exceed adequate levels, experience under our scheme would allow the regulator to determine quickly which parts of the rate structure were above Ramsey levels and which were below. This is true because the proposal contains a systematic bias: imposing the permitted rate increases over several years should permit railroads to achieve a profit-maximizing rate for "lower-rated," more competitive traffic, thereby yielding rates tilted in favor of "high-rated," price-inelastic traffic. In other words, rates on price-elastic shipments would be above the Ramsey level, while rates on price-inelastic shipments —although higher as a percentage of cost than the former—would be below the Ramsey level. This bias is politically convenient in that it favors captive shippers, the loudest complainers about rail rates.

Prospects for Reform

Whether the ICC can be persuaded to adopt a plan of this sort is unclear. It seems likely, though, that the various U.S. courts of appeals —which in an abrupt change of course have consistently ruled against commission decisions in recent months—will force the commission to reconcile its maximum-rate policies with its revenue adequacy principles.

The ICC may also be forced to move toward consistency by the extraordinary size of its pending caseload. The agency is especially ill-prepared to cope with an 800-case backlog at this time. All of its recent attempts to formulate a rate policy based on 7 percent and ton/ton mile formulas have been overturned by the courts. Moreover, its staff has been dramatically reduced in size, its newly developed system for computing variable costs is a shambles, and a majority of its commissioners are brand new to the job.

A final point should be stressed. Central to our proposal is the assumption that railroads can be expected to maximize their profits and that this conduct will lead to socially beneficial results. However, if the railroads are in fact poorly managed and inefficient, as is so widely alleged, the beneficial results will not follow.

Considering the alternatives, we prefer to rely on railroad managers whatever their foibles may be. To permit the ICC or some other governmental body to . . . tell the railroads how to run their businesses would be absurd.

But then, efficiency is a relative concept. Considering the alternatives, we prefer to rely on railroad managers whatever their foibles may be. To permit the ICC or some other governmental body to intervene and tell the railroads how to run their businesses would be absurd. Nor would government ownership of the railroads be likely to increase efficiency, if experience with Conrail is any indicator. Yet another approach would be to keep rail profits abnormally low in order to force the railroads to improve their operations. But that is what the ICC has been doing for twenty-five years—albeit unwittingly, and clearly without beneficial effect. We can only conclude that it is entirely reasonable to give railroad managements the freedom and opportunity to act in their own behalf.

Nearly a century of regulation cannot be reversed overnight. Under our scheme, carriers would have to tolerate a situation where they are legally incapable of achieving revenue adequacy immediately. Shippers would have to wait for their day in court. The commission would have to learn to minimize its interference, or end it altogether. But the pay-off would be worth the price. The country would have a system of economically efficient rates that allowed the railroads to earn the revenues necessary for providing the services shippers require. And we would have found out, at last, whether the achievement of that rate structure requires governmental interference. ■

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Unsnarling the Federal Grant System

Claude E. Barfield, Jr.

In proclaiming deregulation of the federal grant system as a major domestic goal, President Reagan has found a worthy target. The system is huge, costly, and clumsy at furthering its goals of providing services while maintaining the vitality of state and local governments. Yet, despite the attention paid of late to the burden that federal regulation places on business, little note has been taken of similar effects on states, counties, and municipalities. There is, indeed, very little empirical research on the subject. One study, however, suggests the dimensions of the problem. Thomas Muller and Michael Fix of the Urban Institute have estimated the costs of five federal programs—clean air, unemployment compensation, bilingual education, education for handicapped children, and transit accessibility for the handicapped—to the taxpayers of six cities and one county. They found that in 1978 the five mandates imposed an average incremental cost of $25 per capita, essentially the same as the aid the seven jurisdictions received under federal revenue sharing. The authors predicted that such burdens would rise substantially over the next five years. (See "Federal Solicitude, Local Costs," *Regulation*, July/August 1980.)

The vast majority of impositions upon state and local governments are not outright requirements, but rather conditions attached to (presumably) attractive federal grants. In 1980 a research team at the University of California (Berkeley) counted 1,259 federal mandates on state and local governments, 223 of which were direct orders and the remaining 1,036 conditions of aid. Between 1960 and 1980 there was an astonishing explosion of state and local grant-in-aid programs, the number climbing from around 150 to almost 600, and the dollar amount from $7 billion to nearly $83 billion.

Two of the most onerous elements of the system are the so-called crosscutting regulation and the narrow categorical grant. The former term refers to a regulation that applies to the programs (including the grants-in-aid programs) of many agencies throughout the government, meaning—since each agency must ensure compliance with its own programs, according to its own best lights—that there will be multiple, duplicative, and often inconsistent interpretation and enforcement of the same statutory requirement. In its latest reckoning, the Office of Management and Budget (OMB) lists sixty-eight regulations of this kind (see table, page 43).

As for the narrow categorical grant, this has the effect of adding substantially to overhead costs and reducing state officials' ability to match federal dollars to state priorities. There now are, for instance, eleven grant programs for highway safety—including programs on hazardous railway crossings, safer pavement markings, roadside obstacles, bus driver training, bridge upgrading and replacement,

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traffic fatality reduction, seat belt use, and (guess what?) "safer roads." Accompanying these programs are eleven different application forms, eleven different financing cycles, eleven different reporting and audit procedures, and several different eligibility requirements. The task of building a safer highway from here to there, state officials justifiably complain, is itself replete with roadblocks and uncertain crossings.

The Executive Proposes . . .

The Reagan administration has mounted an attack that addresses both of the major problems described above. First, the President's Task Force on Regulatory Relief (chaired by the Vice-President) is trying to scale down the requirements—particularly the crosscutting requirements that accompany grant dollars. Currently, almost 100 crosscutting and program-specific federal regulations are under review. Over time, this case-by-case approach will undoubtedly have an impact. But the sheer number of individual regulatory programs and the time required to change them means that important relief for state and local governments as a product of this effort will be slow in coming.

As its second tactic for reducing the burden on state and local governments, the administration proposes to consolidate, in the next few years, a substantial number of the 600-odd categorical programs into broad grants of authority. The first step toward this end came in January when President Reagan asked Congress to combine eighty-three categorical programs, totaling about $11 billion, into six block grants—for health services, preventive health, social services, local education, state education, and energy and emergency assistance.

Moreover, in the interests of drastically reducing red tape, the six proposals contained many fewer requirements than are customary for block grants. Indeed, although labeled grants, they looked more like President Nixon's special revenue sharing bills of 1971. For instance, there were no provisions for matching funds by the states, no earmarking of particular categories (except for several years in the local education bill), and no obligation for the states to maintain existing levels of effort or funding for a particular program (again except for local education). Funds were to go directly to the states as entitlements, without even a requirement that the states submit to Washington their plans for allocating the funds. The states were to be completely free to allocate resources among the consolidated categorical programs—free to give no funds to some and greatly expanded funds to others.

In addition, while the states would have to publicize their plans for spending the grant funds, they would not have to hold formal public hearings. Also, although they would have to prepare reports on how the funds were used and provide for independent biennial audits, the contents of the reports and audits would be the states' business, not the federal agency's.

. . . and Congress Disposes

But some funny things happened to the Reagan block grant proposals on their way through Congress. Though fifty-six of the eighty-three categorical programs proposed for consolidation ended up in block grants, many of the most important and most expensive did not. There remain, as testimony to committee and special-interest power, separate authorizations for the following: in the health area, migrant health ($43 million), family planning ($143 million), and developmental disabilities ($61 million); in the social services area, foster care ($349 million), child welfare services ($163 million), and rehabilitation services ($931 million); and in education, emergency school aid ($108 million), education for the handicapped ($922 million), and adult and vocational education ($120 million); plus many more. In addition, Congress created some small block grants of its own, among them one for maternal and child health, one for alcohol, drug abuse and mental health, and one for primary care. Thus, both state flexibility and the potential for lower administrative costs were reduced.

Inevitably, also, Congress tacked on to the block grant legislative package a number of conditions and mandates. First, the reports that the states prepare on their use of block grant funds now must set forth specific goals, describe activities to be supported *and* individuals and groups to be served, and analyze the criteria and methods for distributing the funds.

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The states fear that these provisions, despite explicit language in the conference committee report to forestall such a result, will be used by disgruntled individuals and organizations for challenging the legality of state decisions on allocating grant funds. Second, the states now are instructed to hold formal public hearings on their reports. Third, the biennial audits must adhere to standards established by the comptroller general of the United States.

And Congress went further. In addition to the rules that apply to the entire block grant package, it added special restrictions to individual block grants. For instance, states may use no more than 10 percent of the funds for administrative costs in the alcohol, drug abuse, and mental health block grant; no more than 20 percent for administrative costs in the education block grants; and no funds at all for administrative costs in the primary care block grant. The health service grant contains language dictating that federal funds supplement rather than replace state, local, or nonfederal funds. The grants for primary care, for maternal and child health, and for education all require matching funds and maintenance of effort from the states. And finally, the grants for primary care, social services, and home energy assistance all prescribe that the *state legislature* must hold a public hearing on the use of the federal funds.

A Faster Way?

All in all, in sharp contrast to its spectacular triumphs on other aspects of the budget and on tax bills, the Reagan administration can claim only limited success to date in advancing its "new federalism" goals. The President has promised to go "back and back and back" to Congress to remove restrictions from existing block grants and get additional consolidations. But if he persists in trying to deregulate the grant system incrementally, the effort will remain ever vulnerable to the depredations and guerrilla warfare of protective subcommittee chairmen and special interest groups, for whom many of the categorical grants were created. Clearly a more comprehensive, expedited approach is in order. The proposed Federal Assistance Improvement Act of 1981 (S. 807) exemplifies such an approach.

S. 807, which was introduced by Senator William Roth (Republican, Delaware) and five cosponsors, passed the Governmental Affairs Committee unanimously on May 21, 1981. Roth, who chairs that committee, has given it a top legislative priority. The bill would greatly facilitate the accomplishment of Reagan's new federalism goals in two ways—by creating new ways for merging grants and by streamlining the administration of some of the most onerous crosscutting regulations.

Grant Consolidation. First, employing a variant of the procedure used in federal reorganizations since 1949, S. 807 would permit the President to submit to Congress a plan for consolidating categorical programs within a functional area and get final action in ninety days (Title I). Specifically, if the House and Senate committees having primary jurisdiction over the programs in question acted affirmatively or failed to act within sixty days, the plan would automatically go to the floors of the respective houses of Congress; thereupon, if both houses voted for the plan, and the President signed the resulting bill, it would become law. If, however (and this is the Achilles' heel of the scheme), the responsible committee acted negatively within sixty days, the plan would not reach the floor. In other words, as far as the overriding problem of committee bottleneck is concerned, the legislative "trigger" mechanism is an improvement over the present system only in that it would prevent committee control by inaction; but a negative committee vote could still stop the plan. Clearly, this part of S. 807 needs strengthening to give the President a shot at a vote by the full house whether or not the sovereign committee disapproves.

In any event, the expedited procedure would be particularly useful for folding into broad grants hundreds of "policy dwarfs" (to quote OMB Director David Stockman) whose administrative costs are high in relation to average program outlays. There are, for instance, thirty-three environmental categorical grants having a median dollar value of about $8.5 million, thirty arts and humanities programs having a median value of $5.7 million, twenty-nine economic development programs having a median value of $5 million, twenty-one natural resources and development programs having a median value of $9.2 million,

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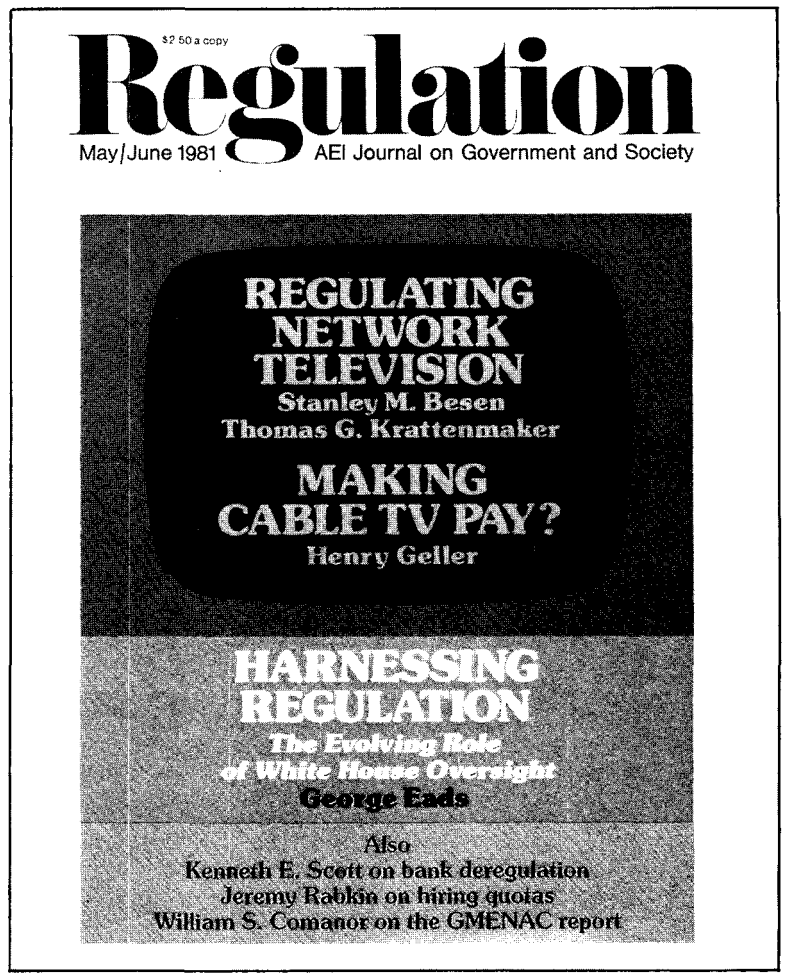

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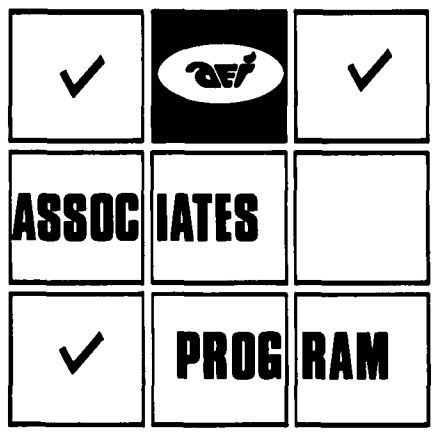

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and twenty criminal justice programs having a median value of $5 million.

Second, the bill would increase the flexibility of federal agencies and state and local governments to use appropriated federal funds in broadly defined functional areas (Title V). Under its provisions, state and local governments would prepare integrated program plans for broad functional areas (generally using the OMB budget categories as guidelines), submit them to the relevant department secretary or agency administrator for approval and, upon obtaining approval, be free to transfer 20 percent of the funds from each categorical program within the particular functional area to meet the plan's priorities. This scheme gets around the narrow restrictions of many categorical grants by allowing the creation of what would amount to temporary and shifting block grants across broad functional areas.

Crosscutting Regulations. S. 807 would also standardize and simplify the administration of crosscutting regulations and reduce the duplication and confusion that result from multiagency enforcement of each crosscutting requirement (Title III). It is estimated, for instance, that there are 150 different program or enforcement mechanisms administered by various agencies in the single crosscutting area of citizen participation. Furthermore, in the case of more than half of the 68 OMB-identified crosscutting regulations, no agency has made any attempt to review its own requirements for potential conflicts with the requirements of other agencies in the same area. Confusion and overlap regarding crosscutting requirements have been a prime factor in the startling rise in litigation involving federal grants that has occurred since 1975.

Because many crosscutting regulations are rooted in legislation, the problems they cause cannot of course be fully solved until Congress provides substantive statutory guidance. Nevertheless, Title III would be a big help in two ways. First, it directs the President to designate a lead agency for each of the following ten subject areas—labor practices, public employee standards, equal services, equal employment, access to government information, procurement, planning, finance and administration, citizen participation, and environmental protection; and it further directs the lead agencies to promulgate a set of integrated standards that would govern all agencies' administration of crosscutting regulations in those fields (unless the President granted a delay because of special implementation problems). Second, Title III provides that a federal agency may establish a procedure for certifying that a state or local government's rules are "at least equal" to the relevant integrated standards. Once certified, existing state and local methods and procedures would remain in effect unless the lead agency could show "good cause" for overturning them.

ENACTMENT OF S. 807 would speed President Reagan's drive to deregulate the federal grant system. Yet throughout the spring administration officials seemed lukewarm toward the bill. In testimony before Congress, OMB Deputy Director Edwin L. Harper noted White House support for the bill's concepts while focusing in nit-picking fashion on details of statutory language that worried the administration. Such seeming ambivalence was caused in part by the priority given to budget and tax matters and in part by the fear that all-out support for S. 807 would jeopardize the six block grant proposals by allowing opponents to suggest that action on those proposals be postponed until S. 807 passed.

With the block grants now enacted, though in much diluted form, the administration would be well advised to rethink its strategy for the coming session. And indeed, it may be in the process of doing just that. On June 3, well after hearings on S. 807 had closed, President Reagan sent a letter to Senator Roth warmly expressing his "personal endorsement" for the bill.

In the coming months, the Vice-President's regulatory task force will continue its case-by-case reviews and, in the process, will undoubtedly bring about the revision or repeal of some regulations that are costly for state and local governments. And the White House says it will propose additional individual block grants to Congress in January. But given this year's record and the vulnerability of the piecemeal approach to entrenched congressional and special interests, the Reagan administration should also put its full lobbying muscle behind a comprehensive approach of the sort embodied in S. 807.

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CROSSCUTTING REGULATIONS APPLYING TO FEDERAL GRANTS

Subject	Authorizing Statute, Executive Order, or Circular	Citation	Agency
	I. SOCIAL POLICY		
NONDISCRIMINATION			
Race	(1) Civil Rights Act of 1964, Title VI Prohibits discrimination because of race in any federally assisted activity.	42 U.S.C. 2000d	Justice
	(2) Executive Order 11246 of 9/24/65 Prohibits discrimination in employment because of race in federally assisted construction.		Labor
	(3) Civil Rights Act of 1968, Title VIII Executive Order 12259 of 12/31/80 Prohibits discrimination because of race in the sale or rental of housing.	18 U.S.C. 245	HUD
Color	(4) Civil Rights Act of 1964, Title VI Prohibits discrimination because of color in any federally assisted activity.	42 U.S.C. 2000d	Justice
	(5) Executive Order 11246 of 9/24/65 Prohibits discrimination in employment because of color in federally assisted construction.		Labor
	(6) Civil Rights Act of 1968, Title VIII Executive Order 12259 of 12/31/80 Prohibits discrimination because of color in the sale or rental of housing.	18 U.S.C. 245	HUD
National Origin	(7) Civil Rights Act of 1964, Title VI Prohibits discrimination because of national origin in any federally assisted activity.	42 U.S.C. 2000d	Justice
	(8) Executive Order 11246 of 9/24/65 Prohibits discrimination in employment because of national origin in federally assisted construction.		Labor
	(9) Civil Rights Act of 1968, Title VIII Executive Order 12259 of 12/31/80 Prohibits discrimination because of national origin in the sale or rental of housing.	18 U.S.C. 245	HUD
Age	(10) Age Discrimination Act of 1975 Prohibits unreasonable discrimination on the basis of age in federally assisted activities.	42 U.S.C. 6101	HHS
Handicap	(11) Rehabilitation Act of 1973, Sec. 504 and amendments of 1974 Prohibits discrimination because of physical or mental handicap in federally assisted activities.	P.L. 93-516	Justice
	(12) Architectural Barriers Act of 1968 as amended Requires that buildings built, leased, or financed with federal aid be made accessible to the handicapped.	42 U.S.C.	ATBCB
Visual Impairment	(13) Education Act Amendments of 1972, Title IX Prohibits discrimination because of blindness or impaired vision in admissions to courses of study by recipients of federal financial aid.	20 U.S.C. 1684	Justice
Sex	(14) Executive Order 11246 of 9/24/65 Prohibits discrimination because of sex in federally assisted construction costing over $10,000.		Labor
	(15) Civil Rights Act of 1968, Title VIII Executive Order 12259 of 12/31/80 Prohibits discrimination because of sex in the sale or rental of housing.	18 U.S.C. 245	HUD
	(16) Education Act Amendments of 1972, Title IX, as amended Prohibits discrimination because of sex in federally assisted education programs including such activities as recruiting, financial aid, student employment, curriculum, athletics.	20 U.S.C. 1681	Justice
Religion	(17) Executive Order 11246 of 9/24/65 Prohibits discrimination because of religion in federally assisted construction in excess of $10,000.		Labor
	(18) Civil Rights Act of 1968, Title VIII Executive Order 12259 of 12/31/80 Prohibits discrimination because of religion in the sale or rental of housing.	18 U.S.C. 245	HUD

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Subject	Authorizing Statute, Executive Order, or Circular	Citation	Agency
Alcohol Abuse	(19) Comprehensive Alcohol Abuse and Alcoholism Prevention, Treatment and Rehabilitation Act of 1970 Prohibits discrimination because of alcohol abuse or alcoholism by federally assisted public or private hospitals or outpatient facilities.	42 U.S.C. 4581	HHS
Drug Abuse	(20) Drug Abuse Prevention, Treatment, and Rehabilitation Act of 1972 as amended Prohibits discrimination because of drug abuse by federally assisted public or private hospitals.	21 U.S.C. 1174	HHS
PREFERENCE			
Indians	(21) Indian Self-Determination and Education Assistance Act of 1975 Requires that federal financial aid for Indian organizations give preference to Indians in opportunities for training and employment.	25 U.S.C. 450b	None
Women	(22) Executive Order 12138 of 5/18/79 Establishes a national program to foster women's businesses by encouraging preference in procurement, in the deposit of federal funds, et cetera.		ICWB
Minorities	(23) Executive Order 11625 of 10/31/71 Establishes a national program to foster minority businesses through preferences to minority owned banks.		Commerce
	(24) Executive Order 12320 of 9/15/81 Requires assistance agencies to establish annual plans for increasing the participation of historically black colleges and universities.		Education
Labor Surplus Areas	(25) Executive Order 10480 of 8/14/53 Executive Order 11051 of 9/21/62 Encourages federally aided activities to use existing plants and workers in labor surplus areas instead of creating new plants or moving workers.		DOD/GSA
PROTECTION OF LIFE			
Human	(26) National Research Act Prescribes ethical procedures to be followed by financial aid recipients when doing biomedical and behavioral research involving human subjects.	42 U.S.C. 289	HHS (NIH)*
	(27) Lead-Based Paint Poisoning Prevention Act Prohibits the use of lead-based paints in housing built or renovated with federal support.	42 U.S.C. 4831b	HUD
Animal	(28) Animal Welfare Act of 1976 Requires humane care of warm-blooded animals used in federally supported research.	7 U.S.C. 2131	Agriculture
	II. ECONOMIC POLICY		
FLOOD INSURANCE	(29) National Flood Insurance Act of 1968 as amended by Flood Disaster Protection Act of 1973 Requires insurance of federally assisted projects built in flood prone areas.	42 U.S.C. 4001	FEMA
TRANSPORT PREFERENCE	(30) Cargo Preference Act of 1954 Requires preference to private U.S. flag vessels in carrying ocean cargoes generated by federally aided activities.	46 U.S.C. 1241	Transportation
	(31) International Air Transportation Fair Competitive Practices Act of 1974 Requires maximum feasible use of U.S. air carriers for international travel paid wholly or partly by federal funds.	49 U.S.C. 1517	GAO
WAGE KICKBACKS	(32) Anti-Kickback (Copeland) Act Outlaws and prescribes penalties for wage "kickbacks" in federally assisted construction.	18 U.S.C. 874 40 U.S.C. 276c	Labor
WAGES/ BENEFITS	(33) Davis-Bacon Act of 1921 Requires that workers on federally assisted construction receive "prevailing" rates and benefits as determined by the secretary of labor.	40 U.S.C. 216a 46 Stat. 1494	Labor
	(34) Contract Work Hours and Safety Standards Act of 1962 Requires that workers employed on federally assisted contracts receive at least one and one-half times their basic wage rate for overtime.	40 U.S.C. 327	Labor

*Acting as informal lead agency.

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Subject	Authorizing Statute, Executive Order, or Circular	Citation	Agency
CONSERVATION	(35) Power Plant and Industrial Fuel Use Act of 1978 Executive Order 12185 of 12/17/78 Requires federally assisted projects to incorporate energy conservation measures.	92 Stat. 3318	OMB
PATENT RIGHTS	(36) Patent and Trademark Amendments of 1980 Gives universities, nonprofit organizations, and small businesses first right of refusal to inventions made in performance of federally assisted R & D.	35 U.S.C. 200	OMB/GSA
	III. ENVIRONMENTAL POLICY		
GENERAL	(37) National Environmental Policy Act of 1969 as amended Requires that federally assisted projects be reviewed to determine whether they will have "significant adverse impact" upon the environment.	42 U.S.C. 4321	CEQ
LAND	(38) Executive Order 11988 of 5/24/77 Requires that proposals for federally assisted activities in a flood plain be analyzed to minimize damage to the flood plain.	42 U.S.C. 4321 42 U.S.C. 4001	WRC
	(39) Executive Order 11990 of 5/24/77 Prohibits federal aid for new construction in wetlands.	42 U.S.C. 4321	WRC
	(40) Coastal Zone Management Act of 1972 Requires that federally assisted activities be consistent with federally approved state programs for protecting coastal resources.	16 U.S.C. 1451	Commerce
AIR	(41) Clean Air Act Amendments of 1970 Prevents violators of Clean Air Act requirements from receiving federal financial aid.	84 Stat. 1707	EPA
	(42) Clean Air Act Amendments of 1977, Title I, Sec. 176c Requires that federally aided activities conform to state implementation plans for attaining national ambient air quality standards and protecting air cleaner than the standards.	42 U.S.C. 7401	EPA
WATER	(43) Federal Water Pollution Control Act Amendments of 1972 Executive Order 11738 of 9/12/73 Prevents violators of Clean Water Act requirements from receiving federal financial aid.	33 U.S.C. 1251	EPA
	(44) Public Health Service Act as amended by the Safe Drinking Water Act Prohibits federal aid to projects that might contaminate an aquifer that is the principal or sole water source for an area.	42 U.S.C. 300f	EPA
	(45) Wild and Scenic Rivers Act of 1968 as amended Requires a finding that federally assisted activities pose no threat to the special values of a designated river or section thereof.	16 U.S.C. 1271	Interior
HISTORIC PROPERTIES	(46) National Historic Preservation Act of 1966 as amended in 1970, 1973, 1976, and 1978 Requires that Interior review federally assisted projects for their impact on properties listed on, or eligible for, the National Register of Historic Places and that, in the event of possible adverse impacts, ACHP agree to a plan of action.	16 U.S.C. 470	Interior/ ACHP
	(47) Archeological and Historic Preservation Act of 1974 Requires that prospective federally assisted projects be monitored to identify eligible historic sites for listing in the National Register.	16 U.S.C. 469	Interior
ENDANGERED SPECIES	(48) Endangered Species Act of 1973 as amended Requires that federally assisted activities not jeopardize any endangered species or its critical habitat.	16 U.S.C. 1531	Interior
	IV. ADMINISTRATIVE POLICY		
GENERAL	(49) Federal Grant and Cooperative Agreement Act of 1977 Establishes government-wide criteria for procurement contracts, grants, and cooperative agreements based on the government's purposes for entering into various transactions.	41 U.S.C. 501	OMB
INDIVIDUAL RIGHTS	(50) Privacy Act of 1974 Limits federal collection, use, and dissemination of personal information, and establishes an individual's right to review his or her records.	5 U.S.C. 522a	OMB
	(51) Freedom of Information Act of 1966 Ensures any person the right of access to a wide range of records related to the activities of federal agencies.	5 U.S.C. 552	None

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Subject	Authorizing Statute, Executive Order, or Circular	Citation	Agency
	(52) Uniform Relocation Assistance and Real Property Acquisition Policies Act of 1970 Provides for uniform and equitable treatment of persons displaced from their homes, businesses, or farms by federally assisted programs.		GSA
PERSONNEL STANDARDS	(53) Intergovernmental Personnel Act of 1970 as amended by Title VI, Sec. 602, Civil Reform Act Ties the eligibility of state and local governments for financial assistance to the establishment of personnel merit systems.	42 U.S.C. 4728	OPM
	(54) The Hatch Act of 1939 as amended Restricts partisan political activity by state and local officials.	5 U.S.C. 1501	OPM
REDUCTION OF PUBLIC BURDEN	(55) Statistical Policy Handbook (formerly OMB Circular A-46). Provides standards and guidelines for the collection and use of statistical data by recipients of federal aid and procurement contracts.		OMB
	(56) OMB Circular A-40 Provides for OMB clearance of proposed agency forms for collecting information from ten or more non-federal persons or organizations.		OMB
STATE & LOCAL	(57) Intergovernmental Cooperation Act of 1968 Prescribes procedures for notifying states of federal actions on assistance applications.		Treasury
ASSISTANCE AGREEMENTS			
General	(58) OMB Circular A-110 Provides guidance for federal direction of assisted research by nonprofit organizations.		OMB
	(59) OMB Circular A-102 Provides standards on administering aid agreements between the federal government and state or local governments.		OMB
Cost Principles	(60) OMB Circular A-87 (formerly FMC 74-4) Provides guidance for determining allowable costs of programs administered by state and local governments under federal procurement contracts and assistance agreements.		OMB
	(61) OMB Circular A-122 Provides principles for determining costs applicable to work by nonprofit organizations under procurement contracts and assistance agreements.		OMB
	(62) OMB Circular A-21 (formerly FMC 73-8) Provides principles for determining costs applicable to work by colleges and universities under procurement contracts and assistance agreements.		OMB
	(63) OMB Circular A-88 (formerly FMC 73-6) Requires single agency responsibility for negotiating indirect cost rates applicable to aid agreements with educational institutions.		OMB
JOINT FUNDING	(64) OMB Circular A-111 Provides policies for projects jointly funded by federal agency and one or more states, local governments, or nonprofit organizations.		OMB
CASH ADVANCES	(65) Treasury Circular 1075 Prescribes practices to prevent premature and excessive withdrawal of funds advanced to contractors and assistance recipients.	42 U.S.C. 4213	Treasury
AUDITS	(66) OMB Circular A-73 (formerly FMC 73-2) Provides agencies with policies for auditing federally sponsored activities under contracts and assistance agreements.		OMB
FEDERAL CLAIMS	(67) Claims Collection Act of 1966, P.L. 89-508 Prescribes standards for agency collection actions.	31 U.S.C. 951	GAO
STATE & LOCAL	(68) OMB Circular A-90 Provides policy for supporting state and local efforts to develop information systems.		OMB

Note: As defined by the Office of Management and Budget, crosscutting regulations are those national policies prescribed by statute, executive order, or circular which apply to the assistance programs of two or more agencies.

Source: Adapted from draft table, Office of Management and Budget, Intergovernmental Affairs Division, September 1981.

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DOES OVERREGULATION CAUSE UNDERREGULATION?

The Case of Toxic Substances

John Mendeloff

In Washington, the reigning view of environmental health and safety regulation is that it has gone too far. And there is an important sense in which that is true. The Reagan administration has considerable justification for resting its program of regulatory relief on the conviction that standards have been set so strictly that benefits often fall short of costs. But it can also be argued that, in another important sense, environmental health and safety regulation has not gone far enough. Indeed, it is likely that the field is characterized not only by too much control but also by too little, and that the former problem is one reason for the latter. Therefore, the best policy may be to increase the pace of standard-setting while, at the same time, decreasing its strictness. That is easier said than done.

Defining the Terms

To begin unscrambling this puzzle, let us first examine the notions of overregulation and underregulation. Sometimes what we call overregulation may simply mean failure to achieve a given health benefit at the lowest cost—that is, the lack of cost-effectiveness. A 90 percent improvement in air quality, for example, might be produced more efficiently by emissions taxes than by across-the-board requirements to reduce pollution by that percentage.

More often, however, overregulation means that the additional health benefits sought from the stricter standard are not significant enough to justify the additional costs. Making such a calculation is especially difficult, of course, because it unavoidably involves deciding what value to put on reductions in illness and death. One approach to this problem has been to examine the so-called risk premiums demanded by workers in hazardous jobs. These have been estimated in a number of studies to range from roughly $200,000 all the way to $5 million for each accidental death experienced. It seems unlikely—although this is admittedly speculative—that workers place a higher value than this on preventing a death that would occur twenty to thirty years in the future, even if the cause of the death were cancer.

What is society in fact paying to achieve health benefits? Looking at standards of the Occupational Health and Safety Administration (OSHA), John Morrall and Ivy Broder have put the average costs per cancer death averted at $20.2 million for the arsenic standard, $18.9 million for benzene, $4.5 million for coke-oven emissions, and $3.5 million for acrylonitrile.

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For the asbestos standard, however—which accounts for almost 90 percent of the estimated fatal cancers averted by these five standards—the estimated costs are below $200,000 and maybe even below $100,000.

It is important to keep in mind that these are *average* costs. In the case of acrylonitrile, for example, it is the average cost of moving from the preexisting exposure level of 20 parts per million (ppm) to 2 ppm. With acrylonitrile and probably with most toxic substances, it becomes increasingly expensive to achieve added reduction in exposure. Thus, the extra cost per death averted in moving from 3 ppm of acrylonitrile to 2 ppm was undoubtedly much higher than $3.5 million, probably at least twice as much. It is this higher figure that is the valuation implicit in a decision to adopt a 2 ppm standard. Thus even if you value preventing cancer deaths at $3.5 million each, you should not support a 2 ppm standard unless the only choices are 20 ppm and 2 ppm, with no options in between. Since the same point applies to the standards on coke-oven emissions, benzene, and arsenic, the overall numbers clearly are very high. Although these figures are subject to major uncertainties, it should be apparent why the overregulation argument has credibility.

Underregulation, for its part, can be defined quite simply as the mirror image of overregulation—that is, a failure to regulate strictly enough when the marginal benefits would exceed the marginal costs. This can include, of course, failing to regulate at all.

Strictness and Extensiveness

The finding that we have frequently set overly strict health and safety standards does not preclude the possibility that more standards would be desirable. One reason is that there are growing numbers of newly identified hazards that have not been addressed at all. Another is that the cost per death averted is strongly affected by how much exposures are reduced. Thus, even if we believe that the typical exposure reduction of 90 to 95 percent usually imposes excessive costs, we might still agree that a 50 percent reduction would be justified.

The casual lumping together of the charges that regulation has been too strict *and* too extensive is particularly unfortunate because it obscures some important relationships between the two issues and, in so doing, some possible remedies. It is generally agreed that where markets "fail" (because of inadequate information and externalities), regulation of toxic substances is *potentially* beneficial. Yet if we expect that the regulatory response will be improper—that standards will not reflect the most efficient approach or will be set far too strictly—we are likely to prefer inaction on the grounds that the net cost of regulating will exceed the cost of inaction. In this manner, overregulation can cause underregulation. And that in turn suggests that the costs of overregulation properly include the potential benefits forgone when we decide that no regulation is better than overly strict regulation.

An important implication of this is that if standards are set more sensibly, with more attention to weighing costs and benefits, we should be willing to regulate more extensively....

An important implication of this is that if standards are set more sensibly, with more attention to weighing costs and benefits, we should be willing to regulate more extensively than we would otherwise. Suppose that an agency, instead of issuing one new standard a year with a reduction of 95 percent, issued five new standards a year with reductions of 50 percent each. It is highly likely that the second approach of regulating more substances less strictly would be the more cost-effective—would lower the average cost for each fatality averted. (Of course, across-the-board reductions will always be less efficient than setting each standard so that its marginal benefits equal its marginal costs.)

Viewed in this perspective, the Supreme Court's recent cotton-dust decision, which restricts the use of cost-benefit analysis in favor of more protective criteria for standard-setting, might actually end up diminishing OSHA's contribution to worker health. OSHA has declared its intent to circumvent the decision and it probably has the ability to do so at least partially—mainly through its determinations of

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what constitutes "significant risk" and "feasibility." To the extent that it does not succeed and is compelled to regulate more strictly than it would prefer, it will probably become even more reluctant to undertake new standards.

The Reagan administration's regulatory policy comes down hard on the side of weighing costs and benefits and maximizing net benefits, but ignores altogether the implications for extensiveness. A comprehensive plan for regulatory reform should simultaneously consider the pace and extensiveness of regulation as well as the strictness of the individual standards. Perhaps the administration's policy is based on the view that agencies have addressed the biggest problems first, so that by now there are few chemicals left that warrant regulation. What can be said about the merits of this view? The fact is, we currently do not know enough to decide whether it is true or whether, instead, many toxic substances are underregulated. That decision would require preliminary benefit/cost analyses of potential regulatory choices, analyses that have not yet been done. Fortunately, my purpose here is less ambitious —to establish that the underregulation hypothesis is plausible, and then to explore some of the causes and possible remedies of underregulation.

Have We Underregulated?

One indication that significant hazards may be underregulated is the growing gap between the number of carcinogenic chemicals that have been identified and the number that have been regulated. More specific evidence consists of the backlogs that have piled up at regulatory agencies, backlogs that are likely to grow because of accelerated industry and government testing and the rapid rate at which new chemicals are being developed. While only about twenty substances have definitely been identified as human carcinogens, several hundred substances have been found to be animal carcinogens. Given that most human carcinogens also cause cancer in animals, the best guess we can make is that it is likely that many animal carcinogens are also human carcinogens. Concern that toxic substances have not been regulated as broadly as they should be does not, it should be stressed, depend on the view that we are in the midst of a veritable cancer epidemic.

In the case of work-place hazards, OSHA has promulgated regulations on twenty-three health hazards. (Fourteen of those—all relatively rare carcinogens—were addressed in a single rulemaking that stopped short of establishing permissible exposure limits.) Meanwhile, the National Institute for Occupational Safety and Health (NIOSH) has recommended more than thirty new or reduced exposure limits that OSHA has not yet addressed. NIOSH—which is required to suggest the most protective achievable standard regardless of cost—has generally called for reductions of 90 to 99 percent for carcinogens and 50 to 60 percent for other hazards. Even if those particular reductions are not appropriate, there would seem to be a strong prima facie case that some reduction in exposure could be justified for some of these chemicals.

Many of the same chemicals are emitted into the ambient air. Thus the Clean Air Act of 1970 (Section 112) calls upon the Environmental Protection Agency (EPA) to list and then regulate hazardous air pollutants. So far EPA has regulated only four—asbestos, beryllium, mercury, and vinyl chloride (the last one in 1976)—while listing three more—benzene, arsenic, and radionuclides. Thirty-six other chemicals remain under study with no regulatory prospects in sight, and hundreds more have never even been considered. EPA's regulatory mandate is even stricter than OSHA's, requiring that standards be set at levels that protect the public health "with an ample margin of safety" and without regard to costs. Because literal compliance with this criterion might require zero exposure in the case of carcinogens, it is hardly surprising that EPA has failed to comply. Environmentalists complain about the extent of the lapses, and businesses complain about overzealousness, pointing to figures that indicate, for example, that the EPA's most moderate option for benzene would on the average cost over $4 million per cancer death averted.

The Toxic Substances Control Act, passed in 1976 largely to fill the gaps in the existing regulatory framework, authorizes EPA to regulate the use of 55,000 potentially hazardous existing chemicals. Rules have been established for asbestos, PCBs, and chlorofluorocarbons. In addition, the act established an Interagency Testing Committee to recommend chemicals

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for testing and authorized EPA to order manufacturers to perform the tests. Every six months since October 1977 the committee has updated its recommendations. But so far EPA, which is supposed to respond within twelve months, has addressed only three of the forty-two items on the committee's priority list. Although the agency is under court order to come closer to the act's timetable, few people expect it to have much success.

The Reasons for Underregulation

Why have OSHA and EPA set so few standards? There are many answers—beginning with the normal start-up difficulties any agency encounters in its initial years, complicated by attempts at both agencies to draw up generic policies for regulating carcinogens. A second factor is the shortage of good personnel, which restricts the scope of activities and increases oversight burdens on top scientific staff. A third factor is the temptation to resist calls for immediate action because of uncertainty about costs, technology, and, especially, health effects.

The desire to wait for better information and the willingness to delay until it can be obtained are both related to the issue of regulatory strictness. Not only is it *desirable,* as discussed above, that there be an inverse relationship between the intensity and scope of regulation, but it also seems politically inevitable. That is to say, in all probability strictness has been one cause of the paucity of new standards. OSHA is a case in point. Until the Reagan administration, OSHA typically sought out the strictest standard that would hold up in court. The need for "substantial evidence" to support such strictness before the court—and (since the mid-1970s) before White House reviewers as well—caused rulemakings to run longer and consume more staff resources than if the reasonableness of the rules had been more readily demonstrable.

For an example of how statutory strictness contributes to delay, take EPA's regulation of vinyl chloride under the Clean Air Act. David Doniger has observed that, because the agency was reluctant "to either flout the literal meaning of Section 112 or to set a standard effectively closing the . . . industries [involved]," it put off setting a standard for almost three years after the discovery that vinyl chloride was a human carcinogen. Section 4 of the Toxic Substances Control Act presents similar problems. According to chemical industry representatives, its rigorous and comprehensive approach prevents EPA from producing more than two or three test rules a year. "Section 4 will work only to the extent it isn't used," says Peter Barton Hutt, attorney for the Chemical Manufacturers' Association—suggesting that informal bargaining agreements between industry and EPA will lead to a lot more testing results than the agency could ever get through formal rules.

In the larger political arena as well, it seems likely that there are long-run trade-offs between intensity and scope. Industry complaints about overregulation are less likely to elicit White House and congressional sympathy when there are only a few highly protective standards to complain about. But the political and symbolic attractions of strict protection may wear thin when that kind of regulation becomes more extensive. Many who would accept a decision to require a major industry to spend $1 billion a year to prevent 100 fatal cancers a year—or $10 million each—would probably balk at proposals to spend $100 billion to prevent 10,000 cancers—also $10 million each. This reasoning suggests the existence of *some* implicit "regulatory budget"—without, however, suggesting what its limits are.

Making Regulation More Extensive

Assuming that it would be good policy to increase the extensiveness or scope of regulation, how could it best be done? In the abstract there are two ways. One is to reduce the resources required for individual rules so that each takes less time. The other is to increase the total resources devoted to rulemaking so that more proceedings can be undertaken at the same time.

Simplifying Rulemaking Requirements. Taking the two approaches in order, can individual rulemakings be speeded up, or is that like trying to speed up a Beethoven quartet by playing it twice as fast? The answer depends largely on whether important new information will be developed during the rulemaking process. If that is likely to happen, quickness could be a

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liability, especially given the difficulties of re-regulating. But based on OSHA's experience, the likelihood is small: while new health information often triggers a rulemaking, such information usually does not appear during the several years between the proposal and promulgation of a rule. Moreover, it would be even less likely to under a proposal for "tiered testing." Because such a scheme involves successive reviews to screen out proposed rules having low net benefits, it would produce more information before publication of the proposed rule. Note, however, that the use of a priority-setting mechanism to make preliminary assessments of the costs and benefits of hazards would itself require additional resources.

Less strict standards would take less time and consume fewer resources because industry is less likely to challenge them. The only major OSHA rule not litigated by industry was the 1977 acrylonitrile standard, which was adopted at the height of presidential concern about regulatory costs and which did not push the required exposure reduction to the limits of technical feasibility. On the other hand, of course, less strict standards are *more* likely to be challenged by environmentalist and labor groups—a response, however, that would probably be less than fully offsetting because those groups have fewer legal resources at their command. As a practical matter, *if* OSHA and EPA could be assured freedom from litigation, the degree of proof they would have to amass would decline and the rulemaking could be hastened. But again, this assurance would be lacking for any particular standard, unless industry on the one hand and labor or the environmentalists on the other could reach some overarching agreement to sue only if certain bounds had been exceeded. And such agreements would be difficult to reach, because they would be difficult to enforce. Enforcement would probably be less of a problem for labor and the environmentalists given their greater centralization and cohesiveness. But on industry's side, almost any maverick firm could afford litigation that would upset any bargains.

Increasing Rulemaking Resources. While speeding up individual rulemakings might produce some gains in extensiveness, greater gains could probably be achieved by doubling or tripling standard-setting budgets. For OSHA and for EPA's toxic substances activity combined, this would entail at most about $100 million. Yet this strategy too faces major problems.

Why should industry groups, which now have a sympathetic ear in the White House, go along? Why should they be interested in trading off a few strict regulations for a significantly larger number of less strict regulations? Why not just oppose the new regulations? Of course, these questions ignore the mixture of reasons—social responsibility, fear of liability, a desire for a competitive advantage—that can spur firms to accept some form and level of regulation, although usually much less than EPA and OSHA have imposed.

One further reason for firms to consider this trade-off could be the desire to weaken statutory barriers to less strict standard-setting. For example, following the Supreme Court's cotton-dust decision, a *Wall Street Journal* editorial called for amending OSHA's mandate to allow the agency to perform cost-benefit analysis. A related factor could be the recognition that, since the President's ear might not always be so sympathetic, explicit statutory constraints on policy makers (cost/benefit-balancing requirements, for example) would be useful in the long run. Whatever the legislative goal, bargaining would be required. Industry groups might decide to delay until after the 1982 elections, hoping that the next Congress will be more hospitable. Or they might conclude that any constraints likely to be enacted now or in the future would be too feeble to justify the concessions needed to bring them about.

In the case of labor and environmental groups, bargaining advocates would have to contend with the symbolism that those groups attach to the idea of strict regulation. And even if that did not prove insurmountable—even if those groups agreed that a more extensive, less strict strategy would produce more health benefits in the short run—they might argue that the stricter strategy would be more protective in the long run. This view would seem to depend on the assumption that new hazards eventually stop emerging and that the years of an individual's life count roughly the same whether they are saved sooner or later.

More practically, it is difficult to negotiate revisions in a statute in exchange for bigger budgets for regulators. Appropriations are an-

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nual and, even though today's increment becomes tomorrow's budgetary base, the increase may not provide enough security to justify giving up valued language, especially in an atmosphere poisoned by mistrust.

Another approach could be to amend the statutes to require that a certain number of hazards be regulated each year (as some have suggested for Section 112 of the Clean Air Act). While this strategy leaves open the problem of having enough funds and people to implement the mandate, the existence of the requirement might make Congress somewhat more willing to provide those needed resources. In the case of OSHA, labor might agree to some relaxation in strictness in return for explicit statutory requirements that workers removed for medical reasons be guaranteed other jobs at equal pay and seniority.

The obstacles to achieving any of these political bargains are obviously substantial. As in the case of another major regulatory change —airline deregulation—success would probably depend on whether people within the administration were willing and able to get the regulatory agencies to begin the process themselves. At the moment the chances for this do not look good. Bigger budgets for rulemaking are not exactly a top priority.

Conclusion

The conceptual argument that the scope and intensiveness of environmental health and safety regulation should be inversely related seems strong. The companion suggestion that, in the past, the intensiveness of our regulation has caused us to forgo substantial health benefits is supported by a much weaker empirical case. What is needed to explore this question further is the same rough-cut benefit-cost analysis that underlies any intelligent decision on what to regulate and how strict to be.

That research deserves a high priority—for it could lead to a regulatory system that produced more health and safety at far less cost to businesses and other private institutions. If all we have done by 1984 or 1988 is reassess the choices of the 1970s, the cry of underregulation could become as damaging in those elections as the cry of overregulation was in the one just past. ■

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Readings
of particular interest

An Early Report on Free Skies

Airline Deregulation—The Early Experience by John R. Meyer, Clinton V. Oster, Jr., Ivor P. Morgan, Benjamin A. Berman, and Diana L. Strassmann (Auburn House, 1981), 287 pp.

The Airline Deregulation Act of 1978 was preceded by a period of "administrative deregulation" in which many of the historical constraints on airline freedom were relaxed. This study examines the effects of deregulation both in the earlier period and in the first two years under statutory deregulation. The authors' task was complicated by a series of market-disrupting events that occurred in the periods under study, such as a rapid rise in the price of fuel, problems with the DC-10, and a general downturn of the economy.

The authors find that, contrary to the expectations of many deregulation proponents, deregulation did not cause a massive reduction in the level of *standard* coach fares, even after controlling for increases in relative wages and fuel costs; real standard coach fares decreased only about 4 percent. But new discount fares carefully targeted at price-sensitive passengers increased overall traffic, so that the real average price per passenger-mile flown declined substantially, by about 17 percent. This change in price structure may have allowed the airlines to increase load levels and profits far more effectively than a simple across-the-board reduction in the standard coach fare. Nevertheless, it was possible that standard coach fares would still be cut, in line with earlier forecasts, as new airline entry and competition proceeded.

Airline productivity gains in the two-year span from 1977 to 1979, a period of first "administrative" and then statutory deregulation, roughly matched the gains during the previous six years under regulation (1970–76), even though there were no major technological sources of productivity gain in the period of deregulation. Some changes in the quality of service complicated matters: crowding may have reduced overall service quality, while more frequent flights may have improved it. The authors speculate that business travelers may have experienced less of a net gain (and possibly even a loss) compared with vacation travelers.

Individual airlines showed a wide range of strategies under both "administrative" and statutory deregulation. Nearly all local service airlines sought to extend their networks geographically, while only Braniff of the trunk airlines sought to do so. Though longer routes are generally thought to correlate with better aircraft utilization, the trunk airlines generally improved the latter without increasing the former.

Under deregulation, the airlines initially chose routes to fit their available aircraft rather than aircraft to fit their routes. This strategy worked so long as overall traffic was rising fast (from 1976 until roughly mid-1979). From mid-1979 on, however, a rapid rise in fuel costs and an economic slowdown caught the airlines with too much wide-body capacity. This apparently stemmed from earlier CAB rate regulations that made long hauls (dominated by wide bodies) much more profitable than short hauls (dominated by smaller planes). The wide-body surfeit stimulated price wars in 1979 and 1980 on transcontinental and other long-haul routes, leaving the formerly less profitable feeder routes to operate in relative tranquility and profitability.

The long-standing tendency for both trunk and local carriers to withdraw from the very smallest communities continued under deregulation. But while a few small cities had losses in scheduled service through mid-1979, far more had gains. Subsequently, the 1980 recession cut into traffic at large and small airports alike.

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The Airline Deregulation Act guaranteed "essential" service to small communities for ten years, but also made it profitable to use smaller aircraft. Commuter airlines flying small prop planes replaced larger competitors on many small-city routes, generally resulting in more convenient departure times, more nonstop flights to the nearest major hub airport, and increased ridership. As one consequence, government subsidies dropped substantially.

While the authors feel that it is too early to draw conclusions on industry structure, larger carriers did not seem to be dominating the industry as of 1979. Mergers apparently had the purpose either of acquiring equipment inexpensively or of expanding routes quickly ("end-to-end" mergers). "Parallel" mergers that might limit competition were not encouraged by the CAB. In markets where only one or two firms had been dominant, their share was somewhat eroded, but in large cities, an increase in the number of carriers did not appear to reduce the share held by the market leaders.

Oil Price Controls in Perspective

The Economics and Politics of Oil Price Regulation: Federal Policy in the Post-Embargo Era by Joseph P. Kalt (MIT Press, 1981), 327 pp.

In the early 1970s, a long history of policies that had promoted the interests of domestic crude oil producers came to an end. Depletion allowances, protection from import competition, and state prorationing restrictions on production were all dropped or severely curtailed. In their place, the federal government established a pervasive scheme of price and allocation controls. That scheme gave way in turn to a system of stiff excise taxes under the Crude Oil Windfall Profit Tax Act of 1980.

In this book, Joseph P. Kalt, assistant professor of economics at Harvard University, dissects the major components of federal oil price regulation during the past decade. The unifying theme that Kalt finds among the successive policies is "a battle over the appropriate distribution of income within society, rather than the manifestation of some massive failure of markets and institutions to allocate the nation's resources efficiently."

The three most important federal initiatives were the "entitlements" program, crude oil price controls, and the windfall profits tax. The entitlement program was in effect from late 1974 through early 1981. It provided hefty financial benefits to selected interest groups, such as small refiners, oil-fired electric utilities, and most notably domestic refiners who used imported crude oil. On average, entitlements paid from one-tenth up to one-fifth of the cost of each barrel of imported crude oil, bringing about an increase in imports of roughly 1 million barrels per day—notwithstanding the official goal of "energy independence."

Price controls on domestic crude oil began with the wage and price freeze of 1971 and lasted until early 1981. Beginning in 1973, the controls took the form of constantly shifting, multi-tiered ceiling prices.

Kalt argues that the combination of controls and entitlements is best viewed as an income redistribution policy, rather than an energy policy. By early 1980, the price controls were extracting income from domestic crude oil producers at a rate of approximately $50 billion a year relative to unregulated market levels. The bulk of this, $44 billion, was allocated to users of crude oil through the entitlements program, to be shared by refiners and ultimate consumers. Some proponents of decontrol have argued that the refiners captured the value of these subsidies, leaving final consumer prices unchanged. But Kalt's analysis of price and import data indicates that the entitlements subsidy did in fact lower prices to oil consumers, with refiners and consumers splitting the subsidy sixty–forty. Overall, taking into account the whole range of special interest benefits from oil regulation, Kalt estimates that as of early 1980 refiners and consumers were receiving income transfers of approximately $32 billion and $12 billion a year, respectively. This redistribution entailed substantial efficiency costs, Kalt says: as much as $3 billion a year for private and public regulatory administration, $5 billion a year (in the final period of controls) in the added amount spent to import oil rather than produce it domestically, and $0.5 to $1.0 billion a year in deadweight waste from excessive oil consumption. Kalt estimates that the deadweight waste under the new regime of excise taxes is in the range of $2 billion to $3 billion a year.

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According to Kalt, the windfall profits tax may not be much of a change, in either its distributional or its economic effects, from the price controls and the entitlements program it replaced. The newer measure's multi-tiered excise taxes closely resemble, in both pattern and effective level, the earlier price ceilings. By holding producers' after-tax prices considerably below market levels—extracting $35 billion a year from domestic crude oil producers—they discourage domestic crude oil production and boost import demand by 1 to 1.5 million barrels a day. Much of the windfall profits tax revenue, moreover, has been set aside for a number of programs designed to benefit the intermediate and final users of crude oil. Decontrol along with the windfall profits tax, Kalt says, represents less of a change in federal regulatory policy than one might have expected.

Clean Air: Implications for Health

Health and Air Quality: Evaluating the Effects of Policy by Philip E. Graves and Ronald J. Krumm (American Enterprise Institute, 1981), 156 pp.

Despite considerable scientific research on the health effects of pollution, there still is no "widely accepted theoretical guide to the nature of dose-response relationships," according to the authors of this book. Hence researchers using the same data can draw vastly differing conclusions, each one offering a dose-response function that seems to fit the data well.

Graves, an economist at the University of Colorado at Boulder, and Krumm, a research fellow at the University of Chicago, here propose a uniform methodology for empirically assessing the health effects of air pollution, and demonstrate its use by examining data on hospital admissions and pollution levels in Chicago. They also examine some of the earlier empirical work that has been done on health effects.

Acknowledging that hospital admissions are only a rough indicator of health effects, the authors argue that other ways of assessing health damage suffer from more serious drawbacks. Animals used in lab tests have respiratory and cardiac systems very different from those of humans. Human volunteers cannot be exposed to high dosages, for reasons of ethics, or to long-term dosages, for reasons of expense. "Cross-section" studies comparing different cities are undercut by the great mobility of the modern population, especially since the individuals most vulnerable to pollution are the most likely to move from a smoggy city. Studies of episodes of unusually high pollution, like those in Donora, Pennsylvania, in 1948 and London in 1952, may not reflect low-level, long-term dangers; moreover, there have been no such episodes since the late 1960s.

The authors' data suggests that at the levels studied, the damage done by a single pollutant increases in a faster than linear progression—that is, that later increments do more damage than earlier increments. The authors also found strong positive interactions between pollutants, so that a higher level of one pollutant increased the damage done by another. "The presence of interactions and nonlinearities," they write, "suggests that uniform standards are an inappropriate means of solving the pollution problem." A city with high levels of several pollutants may be best advised to crack down especially hard on one of them because of the interaction problem.

Pollution levels in large cities have generally come down since the 1960s, notably for particulates and sulfur dioxides, Graves and Krumm note. But most of the improvement can be attributed to some older, lower-cost anti-pollution measures, not to the more stringent rules of later years.

Risk and Regulation: The Food Additive Case

The Strategy of Social Regulation: Decision Frameworks for Policy by Lester B. Lave (Washington, D.C.: Brookings Institution, 1981), 166 pp.

In this book, Lester Lave of the Brookings Institution sets out eight "decision frameworks," six currently in use and two that have been proposed, that agencies could use in making decisions on health, safety, and environmental regulatory issues. He then applies these frameworks to various recent regulatory controversies, most notably those concerning food additives and contaminants.

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Drawing by S. Harris; © 1979 The New Yorker Magazine, Inc.

The six frameworks in current use, ranked roughly according to the amount of data and analysis they require and the degree of flexibility they afford to the regulator, are (1) "market regulation," or leaving private markets to the forces of competition and self-interest; (2) "no-risk" standards such as the Delaney Clause, which tolerate no increase in risk no matter what the cost; (3) technology-based standards, such as those requiring use of a "best available control technology," which need not explicitly take up questions of costs and benefits; (4) risk-benefit, a vaguely specified framework that attempts to balance risks and benefits in a less formal and quantitative way than benefit-cost; (5) cost-effectiveness, which seeks the most efficient means of attaining an objective that has already been defined; and (6) benefit-cost analysis. The two untried frameworks are (7) risk comparison, which weighs the safety risks of various alternatives against each other, and (8) regulatory budget proposals, under which Congress would set annual targets for the burden regulation could impose on the economy.

The Food and Drug Administration is statutorily required to use the "no-risk" framework for carcinogenic food additives, but in fact it exercises considerable discretion. The FDA has moved against three additives linked to cancer in humans or test animals: saccharin, the preservative sodium nitrite, and the livestock feed additive diethylstilbestrol (DES). There is no clause comparable to the Delaney Amendment for carcinogens that occur "naturally." Thus the contaminant aflatoxin, which results from a mold affecting peanuts and some grains, is regulated less stringently, even though it has been linked to liver cancer in both humans and animals. (The FDA did act against another naturally occurring carcinogen, safarole, by banning sassafras tea.)

Each of the possible decision frameworks Lave discusses has its own implications for the control of these substances. At one extreme, no-risk policy would call for bans on all of them. For aflatoxins, however, this is utterly impracticable, since there is no completely effective way to keep aflatoxins out of the food supply; in the field, therefore, the regulator might be forced to move to the less restrictive mode of technologically based standards, including such drastic ones as banning the consumption of peanuts and of corn grown in the Southeast, where the mold is most prevalent. Risk comparison might dictate a ban on saccharin and DES, but not on nitrites, since they protect consumers against the risk of fatal botulism. Cost-effectiveness standards or a regulatory budget might show that consumer health would benefit if the agency shifted its attention from all of these substances to aflatoxins, or perhaps to other health hazards entirely. Benefit-cost, in Lave's estimation, would direct the FDA to leave saccharin alone and to regulate, but not ban, the others; risk-benefit would lead to similar results but with more scope for discretion and ambiguity, since the dollar value of health effects would not be assessed.

In the actual event, Lave notes, the FDA banned DES and saccharin. Congress forestalled the saccharin ban and also forced the agency to back off from tough nitrite regulations. Aflatoxin levels have come under regulation, and the agency has proposed lowering the permitted tolerance level in response to improvements in detection technology.

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Lave concludes that quantitative analysis is feasible not only in the case of additives but for a wide range of other agency decisions as well. It can nudge agencies toward greater economic efficiency, he says, by lopping off the most egregious examples of regulatory excess.

The United States as Common Market

"Regulation, Federalism, and Interstate Commerce," edited by A. Dan Tarlock, principal paper by Edmund W. Kitch (Oelgeschlager, Gunn & Hain, 1981), 167 pp.

Advocates of a strong federal role in the regulation of commerce have warned since the earliest days of the republic that the states, left to their own devices, would erect restrictive barriers to trade, preventing savings from economies of scale and the division of labor. In a series of rulings between 1820 and 1860, the Supreme Court seemed to adopt this view, asserting its right in the absence of congressional action to invoke the commerce clause to invalidate state legislation that blocked interstate commerce. Since then, the Court has come to be viewed as the guardian of the American common market.

This volume contains the proceedings of a conference held in March 1980 at the Law and Economics Center of the University of Miami, sponsored by the Liberty Fund, on federalism and the regulation of interstate commerce. In the conference's principal paper, Edmund W. Kitch, professor of law at the University of Chicago, argues that the Constitution does not necessarily require the Court to maintain free trade between the states, and that the efforts of Congress and the Court to eradicate one kind of barrier to trade have sometimes created different kinds of barriers. For example, congressional jurisdiction over interstate industries such as railroads, interstate trucking, and aviation has led to barriers to entry within those industries that the states themselves might never have erected.

The nation's experience under the Articles of Confederation seems to support the case of the advocates of federal preemption. In the absence of any centralized authority over commerce, states enacted restrictive regulations and taxes to protect indigenous industries and increase state revenues. The *Federalist* refers to the "interfering and unneighborly regulation of some States, contrary to the true spirit of the Union, [that] have, in different instances, given just cause for umbrage and complaint to others."

But Kitch notes that interstate commerce was in fact relatively unimportant at the time that passage was written, because most commerce was with Europe. Many of the restrictions that caused friction between the states pertained more to international than to interstate commerce. For example, some states with major ports levied a tariff on goods brought there from points in other states for export.

Kitch argues that, in theory, states have adequate incentives to cooperate and to promote uniformity of regulation. He cites several examples of state regulations which initially hindered interstate trade but which, with time and under competitive pressure from traders in the interstate market, became less restrictive and ultimately ceased to be barriers at all. "In the short run, this approach to free trade may cause significant bargaining instability, as each jurisdiction tries to establish a bargaining position through bluff, threat, and implemented threat," Kitch says. "But in the long run, this system may provide more free trade than centralized authority because it places stronger incentives on each jurisdiction to promulgate efficient rules for both its internal and external commerce."

The Costs of Product Liability

"Products Liability Insurance, Moral Hazard, and Contributory Negligence" by Richard S. Higgins, in *Journal of Legal Studies*, January 1981, pp. 111-130.

The traditional negligence criterion in products liability law has been giving way to a standard of strict producer liability in the last two decades. Moreover, the defense of contributory negligence, which still survives in some jurisdictions under the names "mishandling" or "misuse," is rapidly being dropped altogether or replaced by "shared liability" rules. Con-

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sumers are, in effect, forced to buy, along with a product, an insurance policy covering injuries from its use. Full producer liability thus amounts to full insurance, while shared liability is similar to a coinsurance or deductible clause.

One theory holds that this shift to producer liability is justified when consumers have less information than producers about product quality and performance and when the information they do have is biased. An opposing line of analysis emphasizes the problem of "moral hazard," the tendency of insurance to make the insured less likely to exercise care, as a reason to maintain partial or complete consumer liability. Richard S. Higgins, an economist at the Federal Trade Commission, outlines a model of product liability that takes into account both biased consumer information and moral hazard, and allows for alternative assumptions about how risk-averse consumers are.

Intuitively, producer liability both lessens the effects of information bias (by incorporating the expected cost of damages in the sale price of the product) and worsens the problem of moral hazard. And Higgins does indeed find that, where moral hazard is absent, consumers who are overly optimistic about product quality will fail under a consumer liability rule to purchase adequate insurance coverage voluntarily. Where moral hazard is present, however, mandatory insurance will often reduce consumer welfare. Even when consumers are overly optimistic, full insurance coverage generally will be less than optimal.

Thus consumer welfare is typically greater, Higgins says, where producers are allowed a defense similar to contributory negligence, in order to deter careless use of products by consumers. A clause wholly freeing producers from liability where the consumer has behaved negligently may be more effective at doing this, and may enhance consumer welfare more, than contributory negligence rules based on either a "deductible" or a "coinsurance" model, Higgins says.

Higgins's model also indicates that regardless of how risk-averse they are, consumers who hold unbiased information about product safety will be better off under consumer than under producer liability. When consumer information is biased, the effects on consumer welfare depend on the relative importance of moral hazard and information bias. The model also implies that the sale price of goods is higher (and fewer goods are accordingly purchased) under producer liability without a contributory negligence rule than under producer liability with such a rule, and higher in the latter than under consumer liability.

Hospital Insurers: Is There a Conflict of Interest?

"Regulatory Control of the Membership of Corporate Boards of Directors: The Blue Shield Case" by William J. Lynk, in *The Journal of Law & Economics*, April 1981, pp. 159-173.

Since at least as far back as 1914, when the Clayton Act forbade interlocking directorates among competing firms, the government has sought to regulate business behavior by determining who may sit on corporate boards of directors. In April 1979 the Federal Trade Commission's Bureau of Competition recommended that the commission venture into uncharted corporate governance waters by barring doctors from sitting on, or controlling, the boards of Blue Shield and similar health insurance plans. In the bureau's view, doctors have a self-evident interest in raising reimbursement rates for their services, so that removing physician influence from Blue Shield boards would remove one upward pressure on medical costs. William Lynk, an economist at Lexecon Inc., here offers evidence that contradicts this view.

Lynk first notes a theoretical reason why physician influence on health insurance plans might not take the form of simple upward pressure on rates. There is substantial variation in physicians' fees, including the fees billed to Blue Shield plans. Physicians are reimbursed at the lower of their actual charge or the plan's reimbursement limit ("allowance"). Lynk points out that each physician would like a reimbursement rate high enough to cover his *own* charges to Blue Shield patients, but no higher, because higher allowances do not benefit him and do make some of his competitors —physicians with higher fees than his—more attractive to Blue Shield patients. Since allowances either above or below the median fee level will be opposed by a majority of physicians,

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physician influence on reimbursement policy should cause allowances to move toward the middle of the fee distribution.

The allowances set by individual plans are ordinarily well above the median charge. But this is due to the demands of the subscribers themselves, Lynk argues. Subscribers who demand comprehensive medical coverage want it to cover almost any physician's charge fully. A majority of physicians, however, would profit from tighter limits. Thus physician influence on a plan should reduce the size of its allowance, not raise it, if Lynk's theory is corect.

Lynk tests the latter hypothesis with three sets of data on Blue Shield reimbursements in 1977. One concerns payments for forty-five medical procedures under a Blue Shield policy available to federal employees throughout the United States. Another is a survey of twenty medical procedures under sixty plans. The third is a survey carried out by the General Accounting Office of reimbursement limits for seventeen procedures. The physician percentage of each plan's board of directors and the percentage of directors who must be approved by medical societies serve as Lynk's measures of doctor influence.

In every instance, Lynk finds, greater doctor influence is associated with lower allowances and lower actual payments. This effect was more pronounced when doctors themselves sat on the boards than when medical societies nominated representatives. Lynk also found that the Blue Shield plans with more doctors on their boards—despite their lower reimbursements—were more successful at getting local doctors to participate. Here, too, direct physician membership had stronger effects than did medical society nomination.

Regulators have directed their attention at the presumed conflict between doctors' and patients' interests, Lynk says. In this instance, however, competition within a group—doctors—appears to be at least as important in determining rates as conflict between groups—doctors and subscribers. If Lynk is correct, efforts to purge doctor influence from the plans may be of little use in lowering health costs.

[EDITOR'S NOTE: *On April 27 the Federal Trade Commission decided not to proceed with a rule on physician participation on Blue Shield boards.*]

No Rule without a Rulemaking?

(*Continued from page 14*)

tion with A, then surely the person who may complain of such unconstitutionality is only B. A has no gripe; he has had his day in court! And Francis Ford, in this case, is A.

There is, however, one basis upon which the Ninth Circuit's holding, though not its reasoning, could be affirmed. A distinctive feature of the case (which the court alluded to, but expressly disclaimed as the basis for its decision) was that, while the adjudication was in progress, a rulemaking was pending on a closely allied subject—*deficiencies* (as opposed to surpluses) in repossession cases. One might well argue that it is irrational, and therefore an abuse of discretion, for an agency to believe that the one problem best lends itself to adjudicatory, and the other to rulemaking, disposition. There would remain, of course, the problem of whether it was the decision to go with rulemaking or the decision to go with adjudication that was bad—but that could be resolved by the presumption in favor of rulemaking established by *Chenery*. ("The function of filling in the interstices of the [Public Utilities Holding Company] Act should be performed, as much as possible, through [the] quasi-legislative promulgation of rules to be applied in the future.") It is by no means certain, however, that even this argument will suffice to keep Francis Ford's chestnuts out of the fire. The agency did in fact offer a plausible reason for treating deficiencies in a rulemaking and surpluses in an adjudication. In its view the "unfairness" of the existing practices was clearer in the latter case (indeed, it thought those procedures actually violated state law). In such circumstances it chose to proceed by adjudication because that would force blameworthy companies to disgorge past profits, while rulemaking would be purely prospective.

Even if the decision in favor of Francis Ford is upheld on account of the parallel rulemaking, the principle thus established would hardly be applicable to many cases in the future. The depressing or encouraging reality is that the reasons for and against the use of adjudication instead of rulemaking are so diverse, so unquantifiable, and so dependent on the facts of the particular case, that the courts are most unlikely to police the selection.

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(Continued from page 4)

Wheeler asks how every cable system could negotiate with every copyright owner for programming rights. How does cable now get the right to present over forty satellite services? Middlemen like HBO, ABC, and Hearst do the job. The real question, which Wheeler will not face and cannot answer, is: in light of the forty satellite services available in the market, why should the government intervene to give cable systems (owned by such "Mom and Pop" outfits as Time-Life, Westinghouse-Teleprompter, and Times Mirror) distant broadcast signals at a government-set, bargain-basement fee?

Wheeler argues that the compulsory license brings non-network programming to communities that would otherwise lack it. That is one reason why cable in the small community should be grandfathered. But surely Wheeler is not arguing that the top fifty markets, with 67 percent of all television households, lack independents.

Ferris argues that the compulsory license is working and that economic studies show no adverse effect on the programmer. The present system is *not* working: sports interests complain bitterly that if they offer an event to one station in one area, it can be shown on cable anywhere, ignoring the wishes of the league or entrepreneur.

Ferris is right to say that I dismiss his cockamamie economic study. I put a question to him, and do so again in vain hope of an answer: If RCA and other videodisc manufacturers asked for compulsory license to use any films they pleased, and had a study done showing "no adverse effects" along with great benefits to, say, rural America, what would he do? And after videodiscs, what would he do when other media came forward with "studies" and requests for government intervention?

It is sad, really, to see these arguments come from Wheeler and Ferris. Wheeler's cable associates were once themselves the victims of market skewing—the pay-TV rules that the FCC adopted to protect broadcasting. Cable had many allies, myself included, in the fight to get rid of these protectionist rules. Now it is cable's turn to skew the market for unfair advantage. The victim has become the victimizer. Ferris, as chairman of the FCC, trumpeted the virtues of the marketplace and deregulation. Now he urges that a government agency, the Copyright Royalty Tribunal, set and adjust the rates cable is to pay for this programming. Some marketplace! Some deregulation!

My original title was "To Market, To Market Goes the Cable Pig." It may have been too long to fit *Regulation*'s cover, but, most unfortunately, it does fit cable.

Affirmative Action for Federal Contractors

TO THE EDITOR:

I hope Jeremy Rabkin ("The Stroke of a Pen," *Regulation,* May/June) is not too disappointed. His article urged the Reagan administration to eliminate, with "the stroke of a pen," the federal government's entire program to encourage the hiring of women and minorities by federal contractors.

Unfortunately for Rabkin, but also unfortunately for many classes of workers still facing employment discrimination in this country, the President's pen subsequently struck through only certain key components of the affirmative action program. Proposed new regulations from the Labor Department's Office of Federal Contract Compliance would exempt all but the largest federal contractors from affirmative action requirements, and would weaken hiring, promoting, and reporting requirements for those remaining.

With a jackhammer repetition of the "quota" buzzword, Rabkin's article drummed up the familiar arguments against government efforts to advance minorities and women into careers that have traditionally been reserved for white men. He could apparently discern no difference between "quotas," which establish an inflexible ceiling for applicants, and "goals," which seek to create a floor for those who have been held down by discriminatory attitudes among employers.

Nobody, I am sure, wants to mandate a ceiling to hold down career advancement. Everybody, I hope, would support a floor to further the attainment of equality of opportunity in our society.

Such floors, or goals, are embodied in the language and the intent of the existing Labor Department regulations. It is ironic that, as these regulations are being effectively enforced, and as increasing numbers of women and minorities are finding employment for the first time in various skilled and professional occupations, a major rollback is being proposed. This is not fair to the victims of continuing employment discrimination. Nor is it fair to the taxpayers whose money would flow to federal contractors hiring and promoting only white males.

Nowhere did I read in Rabkin's article any serious suggestions for bringing equal access to America's work places. It has been obvious since before the Civil War that racism and sexism will not fade away of their own accord. Until someone can bring forward a better alternative, we should stay with the affirmative action plan that is in place and is working.

Shirley Chisholm,
U.S. Representative,
Twelfth Congressional District,
New York

JEREMY RABKIN responds:

Congresswoman Chisholm seems to find something unsporting in my repeated use of the term "quota." Evidently she would prefer that affirmative action policies be described with soothing euphemisms. She would like us to think of affirmative action "goals" as merely a "floor" for some groups—and ignore the plain fact that a floor for some is necessarily a ceiling for others. The congresswoman sees all too well that racial quotas, when honestly acknowledged as such, are repellent to the overwhelming majority of Americans of every personal background.

Quota advocates like Chisholm would have us believe that a spoils system of job allocations by race and sex is the only alternative to passive acceptance of discrimination. I think it is precisely the historic challenge of the Reagan administration to make clear that enforcement of equal opportunity—the right to be considered on one's own merits, regardless of race or sex—is still a realistic alternative, in itself, and in the long run the only workable alternative for a free country. By contenting itself with a few alterations in the enforcement machinery of the contract compliance program, the administration opens itself to the charge of being only half-heartedly for equal opportunity, when it might, by abolishing the quota system, stand forth as its truest champion. Worse, the present course opens the administration to the charge of caring more about the burdens affirmative action imposes on the nation's economy than the burdens it leaves on the nation's soul. ■

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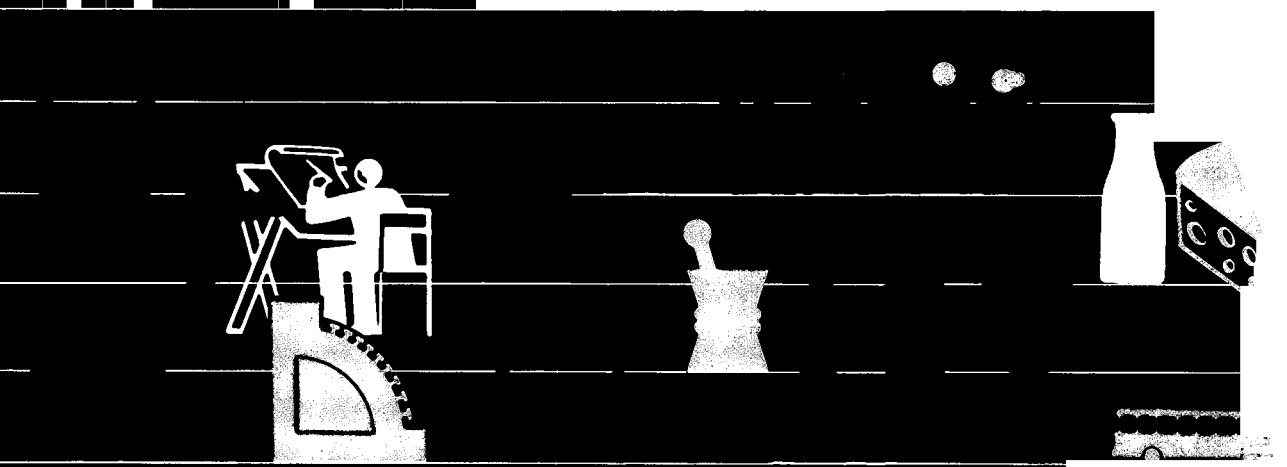

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